BACKGROUND REPORT

EVALUATION OF SME TRADE AND EXPORT PROMOTION IN INDONESIA

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<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
</tr>
<tr>
<td>AICE</td>
<td>Association of Indonesian Coffee Exporters</td>
</tr>
<tr>
<td>BDS</td>
<td>Business Development Services</td>
</tr>
<tr>
<td>BPPT</td>
<td>Agency for Technology Research and Application</td>
</tr>
<tr>
<td>DG</td>
<td>Directorate General</td>
</tr>
<tr>
<td>IETC</td>
<td>Indonesian Export Training Center</td>
</tr>
<tr>
<td>ITPC</td>
<td>Indonesian Trade Promotion Center</td>
</tr>
<tr>
<td>ITC</td>
<td>International Trade Center, Geneva</td>
</tr>
<tr>
<td>ISO</td>
<td>International Standard Organization</td>
</tr>
<tr>
<td>JICA</td>
<td>Japan International Cooperation Agency</td>
</tr>
<tr>
<td>KADIN</td>
<td>Kamar Dagang &amp; Industri Indonesia – CCI / Chamber of Commerce &amp; Industry</td>
</tr>
<tr>
<td>MOA</td>
<td>Ministry of Agriculture</td>
</tr>
<tr>
<td>MOIT</td>
<td>Ministry of Industry and Trade</td>
</tr>
<tr>
<td>MOMF</td>
<td>Ministry of Maritime and Fisheries</td>
</tr>
<tr>
<td>MORT</td>
<td>Ministry of Research and Technology</td>
</tr>
<tr>
<td>NAFED</td>
<td>National Agency for Export Development</td>
</tr>
<tr>
<td>R&amp;D</td>
<td>Research and Development</td>
</tr>
<tr>
<td>SMOCSME</td>
<td>State Ministry of Cooperatives and Small-Medium Enterprises</td>
</tr>
<tr>
<td>TA</td>
<td>Technical Assistance</td>
</tr>
<tr>
<td>UPT</td>
<td>Unit Pelayanan Terpadu – (One Stop Services)</td>
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<td>“Chamber of Commerce &amp; Industry (KADIN) and Associations” – February 2002</td>
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<tr>
<td>World Bank</td>
<td>“Indonesia: From Crises to Opportunity” (non-oil and gas total export), 1999</td>
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V. EXECUTIVE SUMMARY

This background paper discusses and evaluates Indonesian experiences in promoting exports by small and medium-scale enterprises (SME). Attention is paid to both government policies and programs to promote SME exports as well as private sector initiatives.

The main findings of this background paper are:

1. Government-funded programs focus on short-term targets. Government agencies are already happy when they manage to ensure that a SME producer gets an export order. Of course, this is important but, however, it is much more important to develop programs to ensure that SME will have long-term access to export markets. The latter requires also that attention should be paid to quality control, consistency in production volumes and timely delivery of products not only once but also continuously.

2. Most SME exports come from clusters and reach foreign markets through strong involvement of foreign buyers. This offers interesting opportunities for government agencies. Programs do not have to be focused on individual firms but can be effectively focused on clusters of small firms.

3. Current support activities concentrate on promoting and upgrading export capacities of individual firms. NAFED programs are relatively well rated by the SME producers that have participated in its promotional activities. However, there is no attention paid to integrating national and local (cluster-based) associations into SME export promotion programs and activities. The report’s case studies on Associations and Mitra Ventura suggest that there are effective non-governmental Indonesian intermediaries that are successfully linking and matching SME to international markets. They offer both market information and business development services simultaneously. Working through and with associations and other non-governmental intermediaries could enhance outreach, effectiveness and sustainability of public interventions. Such a focus would also encourage networking among firms, support joint marketing efforts and be beneficial for the development of complementary industries.

4. The report highlights the importance of bundled services. It may not be sufficient to offer only information on business opportunities, as being successful on export requires much more. Current export promotion policies, however, lack an integrated perspective that considers R&D, export finance, infrastructure and human resource development, as well as standardization and certification policies as cornerstones of sustainable export promotion. Such an integrated perspective would require intensified cooperation and coordination of relevant public and private actors, and call for restructuring and refocusing the support provided by various government agencies.

5. There is considerable overlap between the export promotion efforts of various ministries and departments. Many public programs appear to have been copied from MOIT and NAFED with regard to both structure and contents. The overlap concerns both export promotion (trade fairs, exhibitions, websites, etc.) and specific trade promotion services to upgrade the capacities of (potential) SME exporters. Overlaps and duplication among line ministries and agencies are creating inefficiencies and wastage of state budgets.
6. The general impression of the report and data analysis is that due to these weaknesses, SME export promotion so far has not been very successful.

It is therefore recommended that:

(1) Export promotion should be embedded into a **wider policy framework** of cluster development, investment promotion and R&D support. Respective strategies should be prepared by stakeholder forums combining relevant public and private sector stakeholders, coordinated by **‘Sectoral Focal Points’** to be created within MoIT.

(2) The rationale for having four agencies promoting Indonesia overseas, namely NAFED / ITPC, MOCSME, BKPM (National Investment Coordination Board) and the Tourism Promotion Board, should be **reviewed**. A closer integration of the a/m agencies would facilitate interaction with Indonesian embassies abroad, as well as reduce overlap in promotion activities.

(3) For **NAFED** it is recommended to **adopt a facilitating approach** that supports delivery of export training through business organizations. Eligibility criteria for support to SME trade fair participation should be sharpened, focusing on 'new-comers' and placing higher relevance on domestic trade fairs. On a medium-term perspective, a stronger role of the provinces in export promotion should be envisaged. The national government should envisage to also promote domestic inter-island trade in addition to promoting exports.

(4) Close the information gap by promoting **public-private partnership in information generation and dissemination**. Match and link activities should be left to business associations and the private sector. The various government websites should be consolidated and refocused, and include links to relevant website content of associations and the private sector (SME Portal). To strengthen the capabilities of business associations in collection and dissemination of market intelligence, it is proposed to set up a **cost-sharing (matching grant) scheme for first-time market research of business associations**.
VI. EXECUTIVE SUMMARY BAHASA INDONESIA

*Background paper* ini membahas dan membuat evaluasi pengalaman Indonesia tentang promosi export perusahaan kecil dan menengah (UKM). Bahasan mencakup baik program pemerintah maupun inisiatif sektor swasta untuk promosi export.

**Temuan utama** *background paper* ini mencakup hal-hal sebagai berikut:


3. Pemerintah seyogyanya membuat kebijakan pemilahan antara UKM yang telah aktif dalam pasar export dan UKM yang baru merencanakan untuk memasuki pasar export. Dalam hal ini saran bagi pemerintah ialah agar dapat menyediakan insentif bagi produk export baru berbasis teknologi yang memberikan nilai tambah yang relatif tinggi termasuk investasi dalam peralatan produksi dengan teknologi yang lebih baik. Demikian pula saran bagi Depperindag dan Menristek/BPPT agar menjalin kerja-sama yang lebih erat dalam pengembangan produk inovatif baru dan teknologi terapan untuk proses produksi yang hemat-biaya tetapi sekaligus meningkatkan kualitas produk untuk menghadapi persaingan global.


5. Terdapat banyak program promosi ekspor yang tumpang-tindih antara berbagai kementerian dan lembaga. Banyak program publik tampaknya disalin dari
Depperindag dan BPEN baik dari segi struktur maupun segi muatan. Program-program tumpang-tindih mencakup baik promosi ekspor (pameran, exhibisi, websites, dll) maupun jasa promosi perdagangan khusus untuk meningkatkan kapasitas ekspor UKM yang potensial. Program-program tumpang-tindih dan duplikasi diantaranya kementerian dan lembaga menciptakan inefisiensi dan pemborosan keuangan negara yang relatif besar.

6. Kesimpulan umum laporan dan analisa data ialah bahwasanya promosi export UKM hingga saat ini, belum berhasil dengan baik

Berdasarkan temuan diatas, beserta ini disampaikan rekomendasi sebagai berikut:

(1) Promosi ekspor sebaiknya tercakup dalam suatu kerangka kebijakan yang lebih luas tentang pengembangan klaster, promosi investasi dan dukungan LitBang. Strategi terkait seyogyanya dipersiapkan oleh forum stakeholder yang menggabung stakeholder relevan dari pemerintah dan sector swasta dengan koordinasi oleh ‘Sectoral Focal Points’ yang harus diciptakan di Depperindag.

(2) Untuk menghindari inefisiensi akibat tumpang-tindah, duplikasi dan pemborosan keuangan negara bagi program-program promosi ekspor UKM, solusi logis yang terdekat ialah semua program promosi ekspor di tingkat nasional hanya dilakukan di satu lembaga, yaitu dipusatkan di BPEN dengan dukungan lembaga PPEI dan ITPC. Program-program BPEN pada umumnya mendapat rating baik dari para produsen UKM yang telah mengikuti kegiatan promosi ekspor BPEN. Dasar pemikiran memiliki empat lembaga yang melakukan promosi ekspor Indonesia keluar negeri yaitu BPEN / ITPC, Menkop-UKM, BKPM dan Badan Promosi Pariwisata, seyogyanya ditinjau kembali. Selain itu, BPEN juga memiliki empat klaster yang dapat menjadi kerangka kebijakan yang lebih luas.


(4) Kesenjangan informasi seyogyanya diatasi dengan promosi kemitraan publik-swasta untuk penyediaan dan diseminasi informasi. Hal ini kemungkinan besar akan dapat tercapai dengan membuat SME Portal yang diusulkan pada tingkat nasional, dibuat oleh SBC (Small Business Council / Dewan Usaha Kecil) dan dikelola oleh BPEN serta kemitraan sector swasta untuk memuat hal-hal yang professional (professional content) serta market intelligence khusus serta peluang bisnis berdasarkan imbalan jasa parsial.

(5) Untuk menguatkan kemampuan asosiasi bisnis dalam pengumpulan dan diseminasi market intelligence, diusulkan untuk membuat skim matching grant (MGS) bagi asosiasi bisnis yang membuat riset pasar pertama kali. Kelayakan penerima skim
matching grant ini seyognya dikaitkan kepada asosiasi bersangkutan yang dapat menyampaikan suatu konsep yang layak untuk diseminasi market intelligence bagi para anggota dan masyarakat luas yang berminat.

(6) Dalam rangka proses penyempurnaan kelembagaan pemerintah dan program, maka berbagai website pemerintah (Deperindag/BPEN, BKPM) seyognya di-konsolidasi dan di-refokus pada penyediaan informasi tentang kegiatan pemerintah, termasuk topik hukum, prosedur ekspor dan pabean, program dukungan dan informasi tentang pameran, exhibisi serta kegiatan serupa. Kegiatan match-and-link seyognya diserahkan ke asosiasi bisnis dan sector swasta. Website pemerintah seyognya membuat hubungan dengan content website yang terkait.

(7) Untuk memperluas jangkauan pelatihan ekspor, disarankan ke BPEN untuk adopsi suatu pendekatan fasilitator. Pelatihan ekspor utamanya disediakan lewat asosiasi bisnis dan Kadin. Dalam rangka tersebut, peran utama BPEN ialah: (i) memelihara suatu database para instructor dan pelatih yang professional dan terakreditasi, (ii) mengembangkan konsep pelatihan, kurikulum dan buku petunjuk, dan (iii) membantu organisasi bisnis dalam hal organisasi dan penyediaan pelatihan ekspor dengan imbalan-jasa yang memadai. Interaksi erat BPEN dengan asosiasi bisnis dengan pendekatan fasilitator diharapkan akan menambah pengetahuan BPEN tentang hambatan-hambatan sector khas dan peluang-peluang yang tersedia.

(8) Perihal dukungan pemerintah untuk partisipasi UKM dalam pameran, disarankan untuk mempertajam criteria peserta dan memberikan prioritas utama pada pameran domestik. Dukungan pemerintah seyognya dibatasi pada 'pendatang baru', yaitu UKM yang ingin ikut serta di pameran perdagangan khusus untuk pertama kali. Untuk membatasi risiko kegagalan, partisipasi dalam pameran di luar negeri hanya perlu didukung apabila UKM telah mengikuti pameran domestik dengan hasil baik dan menunjukkan potensi kesanggupan memenuhi order ekspor berulang kali.

(9) Karena focus dan pasar sasaran sangat bervariasi antara provinsi, dengan suatu perspektif jangka-menengah, diharapkan peran provinsi akan makin besar. Peran BPEN dalam kerangka desentralisasi adalah: (i) menyediakan pengalaman (expertise) khusus dan bantuan bagi provinsi yang ingin memulai kegiatan promosi sendiri; (ii) memberikan informasi tentang pasar dan kegiatan yang relevan, pengembangan perdagangan dalam negeri, secara khusus antara Jawa dan pulau-pulau lainnya. Promosi perdagangan dalam negeri termasuk dukungan keuangan kepada pemerintah kabupaten/kota dan provinsi diberi penggiran untuk mempromosi produk lokal ke pusat-pusat bisnis dan daerah penduduk banyak.
1 BACKGROUND

1.1 Overview of SME exports

Recent export statistics from CBS suggests that Indonesia’s exports during first quarter 2002 dropped 13.8% compared to last year 1st quarter exports. On the supply side the drop is mostly caused by ‘traditional’ factors, such as (i) strengthening of the rupiah exchange rate; (ii) instability of security and law enforcement; (iii) high transaction costs due to corruption; and (iv) frequent labor activities demanding wage increases, and other incentives to improve living conditions due to increased costs of fuel and electricity affecting housing, health, education and consumer prices. On the demand side, the drop of the manufacturing sectors are among others in footwear, fish and shrimp, chemical products, spices, coffee, tea and jewelry which involve mostly SME suppliers. These Indonesian products are losing against similar competitive products from emerging economies such as China, India, Thailand and Vietnam (especially coffee). The drop could escalate if manufacturing industries are relocating to China and Vietnam providing tax incentives, cheaper labor costs, and overall better business environment like law enforcement and security. Anecdotal evidence already indicates that some medium size textile manufacturers have closed their plants in Bandung, West Java, to relocate to China.

Oil and resource-based exports present the greatest challenges to trade promotion because prices and marketing channels are well-established internationally. In 2000, total exports amounted to $65 billion: almost a quarter were oil and gas exports and the rest ($50 million) were non-oil and gas exports. Out of the non-oil and gas exports, around 12 percent include ores and metals (tin and nickel), non-ferrous metals, rubber, logs, pulp and unprocessed agricultural and fish products. These products, as oil and gas, are commodities and hence as such are highly susceptible to fluctuations in international supply and demand. Individual exporters and Government trade promotion initiatives have a limited ability to influence market share and in particular price. The nature of the international market place for these types of products is such that the government’s role is often confined to dealing with government-to-government market access issues (tariff and non-tariff barriers). Active trade promotion may examine the economic constraints to promote processing of these exports in Indonesia. For example, processing of cocoa beans or timber may be limited by size of investment in adequate machinery for processing, among other commodity-specific factors.

Non-oil and gas manufactured exports have greater likelihood to benefit from trade promotion than raw commodities. In fact, most of Indonesia’s non-oil and gas exports are products with some degree of processing or manufacturing (almost 88 percent, see Table 1). For those produced on a contract basis for internationally known brand names, such as electronics and footwear, trade promotion may be limited because these products already have international marketing managed from outside Indonesia. Products with more niche markets could offer more results for trade promotion. Many of these exports are undertaken in sectors that have (or are expected to have) high presence of SMEs, and even microenterprises.
Figure 1: Composition of Non-Oil and Gas Exports, 2000

<table>
<thead>
<tr>
<th>Industry</th>
<th>Exports (US$ Mill)</th>
<th>Share of Total Exports</th>
<th>Potential Presence of SMEs</th>
</tr>
</thead>
<tbody>
<tr>
<td>TOTAL NON-OIL&amp;GAS EXPORTS</td>
<td>47,757.30</td>
<td>100%</td>
<td></td>
</tr>
<tr>
<td>AGRICULTURAL SECTOR ¹</td>
<td>2,728.60</td>
<td>5.71%</td>
<td>High</td>
</tr>
<tr>
<td>MINING SECTOR ²</td>
<td>3,040.80</td>
<td>6.37%</td>
<td>Low</td>
</tr>
<tr>
<td>INDUSTRIAL SECTOR</td>
<td>41,983.40</td>
<td>87.91%</td>
<td></td>
</tr>
<tr>
<td>Fiber, Yarn, Textile and Textile Products</td>
<td>8,182.40</td>
<td>19.5%</td>
<td>Low</td>
</tr>
<tr>
<td>Electronics</td>
<td>7,899.10</td>
<td>18.8%</td>
<td>Low</td>
</tr>
<tr>
<td>Wood Products</td>
<td>4,729.50</td>
<td>11.3%</td>
<td>High</td>
</tr>
<tr>
<td>Steel, Machinery and Automotive parts</td>
<td>3,249.20</td>
<td>7.7%</td>
<td>Low</td>
</tr>
<tr>
<td>Pulp and Paper Products</td>
<td>3,001.90</td>
<td>7.2%</td>
<td>Low</td>
</tr>
<tr>
<td>Leather, Leather Products and Footwear</td>
<td>2,075.40</td>
<td>4.9%</td>
<td>High</td>
</tr>
<tr>
<td>Basic Chemicals</td>
<td>1,957.30</td>
<td>4.7%</td>
<td>Low</td>
</tr>
<tr>
<td>Palm Oil and Products</td>
<td>2,044.80</td>
<td>4.9%</td>
<td>High</td>
</tr>
<tr>
<td>Rubber and Rubber Products</td>
<td>1,320.00</td>
<td>3.1%</td>
<td>Low</td>
</tr>
<tr>
<td>Foods and Beverages</td>
<td>851.7</td>
<td>2.0%</td>
<td>High</td>
</tr>
<tr>
<td>Electrical Equipment</td>
<td>931.6</td>
<td>2.2%</td>
<td>Low</td>
</tr>
<tr>
<td>Copper and Tin Products</td>
<td>936.2</td>
<td>2.2%</td>
<td>High</td>
</tr>
<tr>
<td>Ceramic, Marble, Glass Products</td>
<td>596.9</td>
<td>1.4%</td>
<td>High</td>
</tr>
<tr>
<td>Plastic Products</td>
<td>570.9</td>
<td>1.4%</td>
<td>Low</td>
</tr>
<tr>
<td>Silver, Gold, Precious Metal and Jewellery</td>
<td>500.6</td>
<td>1.2%</td>
<td>High</td>
</tr>
<tr>
<td>Sport Goods, Musical Instruments</td>
<td>482.2</td>
<td>1.1%</td>
<td>High</td>
</tr>
<tr>
<td>Aluminium Products</td>
<td>455.6</td>
<td>1.1%</td>
<td>Low</td>
</tr>
<tr>
<td>Rattan Products</td>
<td>352.9</td>
<td>0.8%</td>
<td>High</td>
</tr>
<tr>
<td>Fertilizer</td>
<td>347.4</td>
<td>0.8%</td>
<td>Low</td>
</tr>
<tr>
<td>Camera and Optical Products</td>
<td>246.9</td>
<td>0.6%</td>
<td>Low</td>
</tr>
<tr>
<td>Cement and Products</td>
<td>189.8</td>
<td>0.5%</td>
<td>Low</td>
</tr>
<tr>
<td>Cigarettes</td>
<td>157.4</td>
<td>0.4%</td>
<td>Low</td>
</tr>
<tr>
<td>Other Chemical Products</td>
<td>184.6</td>
<td>0.4%</td>
<td>Low</td>
</tr>
<tr>
<td>Handicraft</td>
<td>142.6</td>
<td>0.3%</td>
<td>High</td>
</tr>
<tr>
<td>Molasses and Products</td>
<td>128.7</td>
<td>0.3%</td>
<td>High</td>
</tr>
<tr>
<td>Other Products</td>
<td>126.9</td>
<td>0.3%</td>
<td>High</td>
</tr>
<tr>
<td>Medicaments</td>
<td>87.1</td>
<td>0.2%</td>
<td>Low</td>
</tr>
<tr>
<td>Animal Feeds</td>
<td>95.4</td>
<td>0.2%</td>
<td>High</td>
</tr>
<tr>
<td>Essential Oils</td>
<td>56</td>
<td>0.1%</td>
<td>High</td>
</tr>
<tr>
<td>Cosmetics</td>
<td>64.5</td>
<td>0.2%</td>
<td>Low</td>
</tr>
<tr>
<td>Wood Tar, Gum, Gambier Products</td>
<td>18.2</td>
<td>0.0%</td>
<td>High</td>
</tr>
</tbody>
</table>

Source: Central Board of Statistics, processed by Ministry of Industry and Trade, http://www.dprin.go.id

¹ Sixty percent of the sector exports was shrimp (37%), Cocoa (9), coffee (11%), and tuna (5%).
² Ninety five percent of the sector exports was cooper ore (53%) and Coal (42%).
1.2 Presence of SMEs in Export Activity

There is a large literature describing SME presence in export or commodity markets. Differences in the size classification prevent a clear distinction of sectors where SMEs are well-established within a specific sub-sector or commodity. Table 1 summarizes SME presence in some major industrial or manufactured products by indicating whether there is a “low” or “high” potential presence of SMEs, according to many sources. For example, SME exports are expected to be concentrated in the wood products and textile, garments and footwear sub-sectors. Together, some authors (see van Diermen, 1999 and Urata, 2000, based on Ministry of Industry and Trade estimates) estimate that these sub-sectors are responsible for some 50 percent of SME exports from Indonesia. In addition, basic machinery contributes another 16 percent to SME exports. Small holders are important in growing food and cash crops, and there is potential for further SME involvement, however, much of the processing and exporting takes place through larger firms. Overall, a closer look at Indonesian SME exports reveals the following main characteristics:

a. SME exports are concentrated in labor-intensive sub-sectors where low wages are important to enhance the comparative competitive position of foreign markets.

b. Indonesian SME exports are concentrated in clusters. It is well known that SME furniture, garments, and basic machinery production is primarily located in agglomerations of small firms. These clusters are participating in international trade networks to bring down the transaction costs of international trade.

c. SME exports have increased throughout the crisis years due to their relatively limited reliance on imported components compared to larger companies.

In short, most SMEs do not necessarily export their products directly but through trade networks. SME exports from Indonesia are participating in international trade networks in which buyers play an important role in deciding designs, prices, technologies, and timing of production. Such SME are involved in so-called buyer-driven commodity chains. Thus many small enterprises are not directly exporting their products but through the services of intermediaries. Intermediaries link the SME to international markets and they provide a range of bundled services that include pre-financing of production, market access, technology and skills upgrading, advice on designs, advice on patent rights, etc. In such networks, firms and their workers receive compensation mainly for their skills and hours worked. These SME have very limited involvement in activities outside direct production and much of input provision, marketing of output, and also their involvement in upgrading their enterprises is limited with much of the decisions on their development being taken by buyers. This export pattern can be found in such sub-sectors as furniture, garments, etc.

Presently, only the Central Bureau of Statistics makes a systematic distinction between household (cottage), small, medium and large-scale enterprises on the basis of the number of workers. Our focus will be on SMEs and large enterprises, not these micro-enterprises. According to the 1996 CBS census the micro-enterprise sector employs nearly two-thirds of the manufacturing workforce. Despite their large contribution to employment of the latter group, data on micro-enterprises tend to be unavailable in a comparable format to those of more structured businesses. More importantly, promotion of micro-enterprises may not necessarily be a high return activity, such as export activity3, for countries in need for an acceleration of growth (Liedholm and Mead, 1999).

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3 In 1996, census data show that out of 242,030 classified as small firms (that is, micro-enterprises with fewer than 20 workers), only 1,868 had some export activity. See Small Scale Manufacturing Industry Statistics, Jakarta: CBS, Table 28.2, January 2000.
Using the CBS sample by six worker-based size categories (excluding micro-enterprises which have limited export activity), Ter Wengel and Rodriguez (forthcoming) find that, despite the impressive growth in exports by small firms (those with fewer than 100 workers, that is, categories Small 1 and 2), their share of total industrial exports continues to be quite minuscule (see Table 2): It grew from 2.8 percent in 1996 to 4.1 percent in 2000. When medium firms (those with fewer than 500 workers, that is, categories Medium 1 and 2) are added, the share of exports from small and medium-sized firms in total exports shows to be more sizeable: it grew from 28.4 percent in 1996 to 34.4 percent in 2000.

**Figure 2: Exports by Firm Size, Indonesia, 2000**

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(1)</td>
<td>(2)</td>
<td>(1)/(2)</td>
<td>(3)=(1)+(2)/TOTAL</td>
</tr>
<tr>
<td>Small 1</td>
<td>833</td>
<td>1001</td>
<td>83.2</td>
<td>1.3%</td>
</tr>
<tr>
<td>Small 2</td>
<td>1409</td>
<td>2531</td>
<td>55.7</td>
<td>2.8%</td>
</tr>
<tr>
<td>Medium 1</td>
<td>5347</td>
<td>7346</td>
<td>72.8</td>
<td>9.1%</td>
</tr>
<tr>
<td>Medium 2</td>
<td>5652</td>
<td>23958</td>
<td>23.6</td>
<td>21.2%</td>
</tr>
<tr>
<td>Large 1</td>
<td>9985</td>
<td>23440</td>
<td>42.6</td>
<td>23.9%</td>
</tr>
<tr>
<td>Large 2</td>
<td>-6233</td>
<td>64336</td>
<td>-9.7</td>
<td>41.6%</td>
</tr>
<tr>
<td>TOTAL</td>
<td>16992</td>
<td>122613</td>
<td>13.9</td>
<td>100.0%</td>
</tr>
</tbody>
</table>


### 1.3 Overview of Indonesia’s exports in 1st Quarter 2002

- Last year exports statistics from the Central Bureau of Statistics/CBS indicate that the export of manufacturing products has increased by more than 26 percent in the period 1999 – 2000 with substantial growth in exports of garments, furniture and electrical appliances / audio visual equipment. Exports of plywood however declined substantially during this period. Government officials stress that the agreements with the IMF have facilitated exports of unprocessed wood, rattan and bamboo. This has not only hampered the export opportunities for processors of such products, which included many SME but also did not provide added value to the exports of unprocessed products. As mentioned in above 1.1. Overview, Indonesia’s SME exports are rather dependent on exchange rate fluctuations and a limited number of markets.

- Recent export statistics from CBS suggests that Indonesia’s exports during first quarter 2002 dropped 13.8% compared to last year 1st quarter exports. On the supply side the drop is mostly caused by ‘traditional’ factors, such as (i) strengthening of the rupiah exchange rate; (ii) instability of security and law enforcement; (iii) high transaction costs due to corruption; and (iv) frequent labor activities demanding wage increases, and other incentives to improve living conditions due to increased costs of fuel and electricity affecting housing, health, education and consumer prices.

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4 Small 1 – From 20 to 49 workers; Small 2 – From 50 to 99 workers; Medium 1 – From 100 to 199 workers; Medium 2 – From 200 to 499 workers; Large 1 – From 500 to 999 workers; Large 2 – Above 1000 workers.
On the demand side, the drop of the manufacturing sectors are among others in footwear, fish & shrimp, chemical products, spices, coffee, tea and jewelry; mostly involving SME suppliers; who are loosing against similar competitive products from emerging economies such as China, India, Thailand and Vietnam (especially coffee). The drop could escalate if manufacturing industries are relocating to China and Vietnam providing significant tax incentives and cheaper labor costs, including better business environment like law enforcement and security. Already ten medium size textile manufacturers have closed their plants in West Java, relocating to China.

1.4 Notes on SME exporter constraints in access to credit

In general, banks in Indonesia issue commercial credit based on the 5-C principle. In addition to the Character principle, two other C-factors are Collateral and the Capacity of the debtor to repay the loan. Although Collateral is often mentioned as the last resort, in reality banks are strictly holding to Bank Indonesia’s Decree No.31/147/KEP/DIR re quality of productive assets (KAP) and Decree No.31/148/KEP/DIR – 12 November 1998 re productive assets reserves (PPAP). These two decrees were issued with the intent to maintain prudential banking principles at the onset of the financial crisis. Decree No. 31/148/KEP/DIR comprise general reserves to cover possible risk losses while collateral should be used as a subtracting variable (of PPAP), comprising:

- Giro, deposits, savings, and guarantees in Rupiah and foreign currency denominations, withheld (blocked) with power of attorney for 100% disbursements.
- SBI (Bank Indonesia Certificate) and SUP (Government Debt Paper), max. 100%.
- Marketable securities actively traded in the financial markets, max. 50%.
- Land, building, houses, aircraft, and ships over 20 cubicmtrs size, appraised for a maximum value of: (i) 70% within 6 months of date of appraised value; (ii) 50% between 6 to 18 months of date of appraised value; (iii) 30% between 18 to 30 months of date of appraised value; and (iv) 0% over 30 months of date of appraisal.

Conclusion:

Under the given regulatory framework SME exporters experience difficulties to comply with collateral conditions in line with Bank Indonesia guidelines. In general, SME are holding only a Purchase Order (PO), a sales contract, and a L/C, obtained from a trading house or buyer. Banks are usually using these instruments for analyzing the business prospect or cash flow of the SME5. It would be more prudent for banks to avoid disbursing credits to SME involving huge reserves, and instead, buy SBIs (Bank Indonesia Certificates).

Over the past two years, most trading houses in Jepara and Yogyakarta (wooden furniture clusters in Central Java) have no more long-term Sales Contracts from buyers or buying agents in Indonesia. In general, current orders are Purchase Orders detailing number of containers, and time completion, usually within 1 – 4 months. For credit analyses of current one-year loan policy, banks need data and information on past performance and business prospects, at the least for the one-year loan period. Trading houses could easily provide data on past performance but it would be very difficult to make business projections over the 4-months business cycle. These factors impede the credit review of banks resulting in constraints for SME to access bank loans.

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5 This information is also relevant with the study on “The possibility of utilizing Sales Contracts or Purchasing Orders as Credit Security” by CESS in cooperation with Swisscontact and The Asia Foundation (2000)
2 GOVERNMENT SUPPORT FOR SME EXPORTS

There are several government departments and agencies involved in promoting SME exports. The main actors include the National Agency for Export Development (NAFED), the Indonesian Export Training Center (IETC) and the Export Promotion Board, all belonging to the Ministry of Industry and Trade. Below we will first present the main programs and subsequently present comments and an assessment.

2.1 National Agency for Export Development (NAFED)

Established in 1971, NAFED's expert staff has built up 30 years experience in assisting thousands of companies, large and small, to sell their products in world markets. NAFED maintains a comprehensive database of thousands of companies and its main task and functions are to:

a. Formulate policies and establish guidelines for encouraging and supporting the expansion of non-oil & gas exports.

b. Provide information services and technical advisory services for export development.

c. Coordinate and implement export promotion.

d. Expand the range of export products and markets

Its tasks and responsibilities are updated on a regular basis and presently include:

(1) **Target group & capacities.** NAFED does not focus explicitly on SME and, in principle, it offers its services to all Indonesian companies. However, in reality its most prominent customers are SME that are active on export markets since larger firms have developed their strategies and networks to promote their products on international markets. Total budget of NAFED is Rp. 20.5 billion in FY-2001 and it employs some 400 staff members. In addition, NAFED includes a Center for Information and a Training Center.

(2) **Export information.** NAFED has developed an export information network through their website [http://bppei.com](http://bppei.com) that provides information on market opportunities and methods of penetration for Indonesian exporters. Indonesian firms can get free access at present although there are plans to introduce fees for the use of this service. It gets also information on fairs and exhibitions through Indonesian Embassies and for the year 2002, NAFED has already prepared a full scheme of domestic and overseas trade fairs, including seminars and workshops for exchange of trade information.

(3) **Product adaptation.** Product adaptation and development deals with a whole range of issues, from quality and appearance to materials, processing, production equipment, packaging, style and modeling. By working with NAFED, many Indonesian firms are able to advance their programs and activities for adapting and developing existing new products. In 1999, NAFED coordinated discussions, product adaptation clinics and consultations, meetings about partnership developments and cooperative arrangements, involving hundreds of local firms. Partnership development was concerned with assisting SME through linkages with larger enterprises with funding and distribution, thus enabling the appropriate products of the smaller partners to conform to market demands.

(4) **Buyers Services.** Through its Buyers Reception Desk, NAFED aims to assist buyers to reach targeted Indonesian products and potential suppliers including arranging meetings and trade contacts between buyers and exporters taking place at its own offices. It has prepared a number of directories that provide information on Indonesian
companies including their ISO status. For example, recently, a group of buyers from India visited the offices of NAFED to request information on handicraft producers from Indonesia. NAFED organized and chaired a meeting between buyers and exporters. In 1999, the service assisted more than 4,000 buyers. On average, NAFED handles 2,500 enquiries from overseas buyers each year while Industry & Trade Attaches at Indonesian Embassies handle a further 12,500 enquiries each year.

(5) **Export promotion.** NAFED runs an export promotion program, which includes participation in trade exhibitions and trade missions, and linking buyers and potential exporters. Each year, NAFED organizes selling missions to overseas export markets and in most cases; government ministers and officials and representatives of other business interests, such as the Investment Coordinating Board, banking and other services, accompany exporters.

(6) **Trade fairs.** The agency finances the stands and their construction for SME entrepreneurs participating in international trade fairs except for tickets and accommodation, paid by the entrepreneurs themselves. So far, NAFED finances the participation of individual entrepreneurs and *not* of representatives or sector associations of SME.

(7) **Regional units.** NAFED is organized in regional units centers hosted by the respective representative offices of MOIT (Dinas Perindag in current decentralization era in the provinces), who are responsible for promoting Indonesian exports to specific markets, such as Africa and the Middle East, America and Australia, etc. The regional units execute market reviews on a regular basis that focus on issues such as business opportunities, strengths and weaknesses of Indonesian exporters, and identification of export barriers. NAFED buys trade statistics from ITC in Geneva. These are of interest to Indonesian exporters but the data are some 2 years old, which limits their relevance for the identification of current and future business opportunities.

(8) **IETC (Indonesian Export Training Center).** NAFED also runs an export-training center. It provides training programs of three months for entrepreneurs on the management of export and import business and it is specialized in garments and wooden furniture merchandising. It also offers shorter training programs on topics such as export procedures and payment terms, product quality control, participation in trade fairs and exhibitions, and international business communication. The instructors are professional business managers contracted for teaching and therefore IETC has a wide clientele of participants from the business world. The training center has received technical and financial support from various donors among which Japan features prominently. Future plans and development of regional training and promotion centers will be discussed below. There are a number of JICA experts attached to the training center.

The catalogue for 2002 provides an overview of the courses that are offered. It includes a variety of 2,3 and 10 days courses for both potential and existing exporters. The following overview summarizes some of its main courses:

- a Export procedures
- b Letter of credit negotiations
- c Internet as a trade instrument
- d Negotiations
- e Garment merchandising
- f Wooden furniture merchandising
- g Management of stands at exhibitions
- h Quality control
- i Design of furniture and handicraft
- j Export marketing strategy
Fees for participation are on average Rp.100,000 ($10) per day indicating that participants are subsidized. Recently, NAFED paid special attention to provision of courses on contract enforcement as it is confronted with an increasing number of Indonesian exporters that do not have sound business contracts on which they can rely whenever foreign buyers do not perform in accordance with purchase agreements. NAFED considers further to develop this service by sponsoring the screening of contracts by law consultants.

IETC with JICA assistance is opening branches in Surabaya (East Java) by July-2002, Makassar (South Sulawesi) and Medan (North Sumatra) in 2003, and Banjarmasin (South Kalimantan) in 2004.

(9) **ITPC.** Prior to the crisis in 1997 NAFED operated some 13 Indonesian Trade Promotion Centers in 11 countries. The financial crisis urged the agency to close down its centers. Presently, it is reopening some of the centers in Osaka, Los Angeles, and Dubai. NAFED is happy with the performance of the ITPC in Osaka, which has resulted in US$ 1.7 million in orders since it was reopened about a year ago. Interestingly, NAFED explains the good performance of the Osaka center to the fact that Japanese businessmen are used to deal with (semi-) government agencies in international trade relations.

(10) **Website.** NAFED operates a website [http://www.bppei.com](http://www.bppei.com) in both Indonesian and English language. It provides a.o. an overview of trade fairs and exhibitions in Indonesia for the year 2002. The website provides also an overview of international fairs indicating whether NAFED intends to participate actively or passively. Furthermore, the website includes a section on business opportunities in all Indonesian provinces. The English website uses the Indonesian names of provinces. Information on business opportunities at the provincial level is very broad only. It specifies products that are available at the provincial level by alphabet. For example, for Central Java, it mentions under “V” items such as ‘vegetables’, ‘vegetable seed’, ‘VCR’, ‘various glass handicrafts’, etc. The site also provides information on the training center that was visited by some 15,000 visitors since January 2000. Finally, the website provides a platform for discussions that is only available for registered members.

**Evaluation.** The Padjadjaran University in Bandung, West Java, has evaluated the activities of NAFED (2000) on request of the agency. The evaluation includes interviews with 77 entrepreneurs that have made use of services offered by NAFED. The study of Padjadjaran University found that entrepreneurs were reasonably satisfied with the services of NAFED. A main complaint is however, that services are not bundled. For example, some entrepreneurs found that, through participation in a training program, they received useful information on identification of business opportunities. However, the training did not include practical guidelines on how to make use of these business opportunities to increase exports.

The evaluation report also pays specific attention to the impact of participation in trade fairs on the performance of firms. It found for 1999 that NAFED has supported about 500 enterprises to participate in domestic trade fairs and another 380 enterprises on international trade fairs. The study indicated that participation in domestic trade fairs had a greater impact on increased sales compared with joining international fairs.

NAFED is also aiming at generating income sources. Presently its services are offered free of charge. It aims at generating 5 percent of its budget in the coming years through payment for its services.

**NAFED’ plans for the future**

NAFED’ future plans are, to an important extent, based on a number of JICA studies that aim at outlining an export promotion strategy for Indonesia. The JICA / NAFED study
identified the need for government-supported agencies that link and match (Japanese) buyers to Indonesian producers. The study is based on field interviews with selected entrepreneurs in (i) garments and textiles, (ii) food processing, (iii) wood products and furniture, (iv) electrical and electronic parts, and (v) automotive parts. The study concluded that Japanese buyers are not very familiar with Indonesian products. It is very common for sales representatives from various countries to visit Japan but this appears to be less the case for Indonesian representatives. Thus the study concluded that the main problem to be addressed by Indonesia is in marketing and bringing producers in closer contact with buyers so that they can learn from the latter's experiences, requirements, and needs. This is considered to be a prerequisite for effective and well-targeted financial support, human resource development, etc.

The study calls for the development of regional export training and promotion centers that play a leading role in linking producers to international markets, especially for entrepreneurs outside the Jakarta area. These centers shall be financed by the provincial authorities (operational costs), Japan (information technology infrastructure), and NAFED (upgrading, renovation of building).

JICA has played an important role in the design of these centers that are based on two basic notions:

a. Government agencies need to play a leading role in linking and matching buyers and Indonesian exporters
b. Government agencies need to play a leading role in linking and matching buyers and Indonesian exporters

The Master Plan for the development of Regional Export Training and Promotion can be summarized as follows:

a. The main focus of the regional centers shall be SME export promotion to support decentralization processes and facilitate international buyers and (potential) exporters outside Jakarta. Regional centers shall be set up in Surabaya (East Java in July 2002), Medan (North Sumatra) and Makassar (South Sulawesi) in 2003, and Banjarmasin (South Kalimantan) in 2004, while one in Yogyakarta already exists. As mentioned above, the centers are expected to become increasingly financially sustainable. Management of the centers will be the responsibility of the government for at least four years.

b. Main activities envisaged for the centers are similar to those that are presently executed by the national center in Jakarta. Various training activities are planned on export procedures, contracts, business communication, etc. In addition, trade and market information will be provided to both buyers and Indonesian entrepreneurs. The center will have consultancy units that provide producers with advice on how to overcome technical and financial constraints to export trade. Training and consultancy will be the key activities of the regional centers including long-distance training.

c. The centers are to be staffed and managed in accordance with the business opportunities of the regions in which they are located. Each center will, at least, include a chief advisor, coordinator, marketing analyst, information technology expert, and training expert. Each center will have a total staff of some 10-14 persons. Some of the staff members will be trained in Japan. In addition, there will be short-term experts attached to the centers in accordance with local needs and preferences.

2.2 SME exports promotion by other Directorate Generals within the Ministry of Industry and Trade

Activities. Within the Ministry of Industry and Trade there are various Directorate Generals /DG that promote, directly or indirectly, SME exports. DGs such as metal,
machinery and electronics, and chemicals, agro – and forestry products aim a.o. at strengthening the competitive position of small firms in both domestic and export markets. The DGs concentrate on technology upgrading. In addition, the DG International Trade is active in all provinces to develop internationally accepted (ISO) quality control and product testing methods in all provinces. These activities do not focus specifically on SME but experiences show that these enterprises are the main users as larger firms appear to make use of private sector facilities. In addition, there are some programs of the DG for Small and Medium Industry and Trade that also concentrate on the promotion of SME exports. For example, there are activities aimed at the strengthening of subcontracting linkages between foreign firms and SME.

Programs. In general, the programs of the DGs are diverse and frequently include support to SME that are either in the planning stage or already involved in export trade. It is mainly technical support with attention for product development, testing, and quality control. The DGs concentrate on the development of SME through a sector approach that aims at upgrading products and designs. The DGs do not have regional orientation such as NAFED. Export promotion, marketing, linking and matching foreign buyers and traders falls under the responsibility of NAFED.

International trade. Lastly, the DG for International Industry and Trade Cooperation has the responsibility to negotiate Indonesian trade conditions in multilateral and bilateral trade agreements. In addition, the DG is active in exploring multilateral and bilateral schemes to support SME in Indonesia. For example, the Asia – Invest scheme of the European Community financially supports partnerships between European small firms and their Indonesian counterparts. There is also a German – Indonesian Forum, which provides similar support. The DG notes that Western initiatives increasingly want to involve private sector institutions in the formulation and execution of such projects and programs. However, the DG is of the opinion that Indonesia at present does not have sufficiently qualified private sector institutes and government agencies might still be the best counterpart, for the time being.

2.3 SME export promotion by the Ministry for Cooperatives and SME / MOCSME

The Ministry has its own deputy for SME export promotion. The following are FY-2002 programs, which receive high priority of the SME promotion through the Deputy Minister for business networking and marketing:

The FY-2002 programs to improve SME-C skills for export trading comprising:

Programs designed at central level and implemented at national level with central budgets:

a  Expanding export markets of SME-C by developing trade missions and exhibitions;
b  Developing an information system and publication on export markets;
c  Developing franchising in the context of ASEAN cooperation;
d  Developing cooperation between SME-C and TNC/Trans National Corporations;
e  Developing business networking through industry clusters; and
f  Developing partnership models export-oriented SME-C.
Programs designed at central level and implemented at regional level with de-concentrated budgets:

a. Developing SME-C with a cluster-based approach to improve local export potential;
b. Provision of facilities for SME-C to increase exports;
c. Developing export-oriented production centers/clusters.

**Access to finance.** SME receive on average some 20 percent down payments from buyers. This is frequently not sufficient to execute export orders smoothly and additional credit would be welcome. Presently, banks are reluctant to lend to SME. The Ministry supports the establishment of a credit guarantee scheme to improve the access of SME to trade credit.

The Ministry also operates a business information desk that provides data on export business opportunities to SME. The data are partly derived from the same national and international sources as the NAFED information. In addition, the Ministry has developed its own data sources.

**MTAP.** The Medium–Term Action Plan of the Task Force for SME Development stresses the need for incentives for SME export development. More specific, the plan document highlights the need to:

a. Provide incentives to SME entrepreneurs to develop their skills and become more competitive in export markets. In particular, the plan stresses the importance of incentives for the upgrading of the technological capabilities of SME to remain competitive in international markets.
b. Strengthen public agencies that support SME exports especially by the smallest enterprises.
c. Privatize public agencies that support exports by larger SME.
d. Promote the development of private support agencies for SME development.

### 2.4 BKPM / Investment Coordinating Agency

The main task of the Agency is to promote investment at a national level for all regions and it maintains a website with some interesting features, among others:

1. Geography of provinces including information on potential natural resources for possible business development;
2. Information on accessing IPRs (Intellectual Property Rights).
3. List of **Matchmaking On-line Participants** in which overseas and domestic participants exchange information and express their interest for:
   - Specific Indonesian export items;
   - Business opportunities for investment;
   - Partnership possibilities to improve Indonesian exports in terms of product availability (volume), product quality, financing, and markets.

The feature provides a broad range of contacts between overseas buyers or investors and Indonesian exporters or manufacturers (with full style addresses) and indirectly also
opening business opportunities for SME. Hundreds of overseas enquiries are providing useful information if SME and their associations can tap into this website to explore export opportunities or developing export capacities and markets for their specific products including business networking and possible partnerships.

2.5 Assessment of Government SME export promotion efforts

There are only few studies that allow us to evaluate the impact of various programs and projects on SME export promotion based on field observations. Available reports and discussions with SME experts and practitioners lead to the following conclusions:

(1) **SME Exports.** An assessment of government efforts to promote SME exports should take into account that Indonesian SME exports have remained virtually unchanged throughout the years. SME exports have increased in the immediate aftermath of the crisis due to their limited dependence on imported components and formal bank credit. However, the general impression is that SME export promotion has not resulted in a substantial increase in SME exports. There is little or practically no added value in most SME exports of half-finished products or of low quality requiring further finishing.

(2) **Overlap.** There is considerable overlap between the export promotion efforts of various ministries and departments. Many programs appear to have been copied from MOIT and NAFED with regard to structure, methodology and contents.

(3) **Sub-sectors.** Main promotional efforts have a regional orientation with specific sections of departments or agencies focusing on a selected number of provinces. Data suggest that Indonesian SME exports stem from a limited number of sub-sectors and are exported to a limited number of countries. The reopening of some international promotion centers (ITPC) may contribute to increased exports to targeted countries but, so far, their contribution to export promotion is limited. There appear to be no specific programs to promote SME exports by sub-sector despite the fact that specific sub-sectors are very important for SME exports.

(4) **Increased sales.** NAFED programs are relatively well rated by the SME producers that have participated in its promotional activities. Its outreach is however limited and annually only a few hundred producers receive NAFED support. Interestingly, a survey among SME producers suggests that participation in domestic trade fairs contributed most to increased sales.

(5) **Websites.** There are several websites that are promoted by government agencies to promote (SME) exports and distribute information about overseas business opportunities. Both the evaluation study of the Padjajaran University and scattered information from own interviews suggest that these websites are mainly used to learn about trade fairs and exhibitions. The information is used to prepare requests for subsidized participation. The websites are not frequently used to identify new business opportunities mainly because the information is most often outdated. BKPM website has never been explored by SME and their associations.

(6) **Cluster network.** All departments and agencies concentrate their promotional efforts on support to individual SME. There are no specific programs that support business networks or clusters of SME though both are important for successful participation in export markets. Apparently the various export promotion agencies are not (yet) aware that cluster networks of SME could provide synergies of capacities, better efficiencies and may reduce transaction costs. In addition, there is little cooperation between the government export promotion agencies and private sector associations.
3 PRIVATE SECTOR INITIATIVES TO PROMOTE SME EXPORTS

A number of private institutions were visited during September 2001 to gain insight into their role in stimulating exports from Indonesia. We concentrated our visits on SME promotion. Most private institutions that were visited concentrate on the promotion of specific types of products only such as handicrafts, garments, or coffee. Below we present a brief overview of the institutions that were visited before we provide an assessment of the role and importance of private sector institutions in SME export promotion.

3.1 SME exports: the ‘traditional’ view

During our mission we visited the Indonesian Association for Small Enterprise exports that is linked closely to MOIT/NAFED and other departments. In the past, it has been invited frequently by the government to participate in domestic and international trade fairs. Government agencies paid for almost all costs of SME participants to trade fairs. Participation in fairs did result in new orders for selected participants but this has not been a sustainable increase. Most of the orders were for specific orders without the perspective of repeat orders. It concerned mostly traditional Indonesian handicrafts. In recent years, the handicraft association has been invited on an occasional basis only to participate in fairs and exhibitions with government sponsorship.

The association has access to a limited number of new orders but it is not able to execute most of them due to lack of working capital to pre-finance production. Pre-shipping credit is the main obstacle. In recent years access to credit has declined significantly. In the present situation the association has to rely mostly on wholesalers who are in a better position to raise capital to finance production. It is felt that dependency on wholesalers has a negative impact on the profits of SME producers. The association finds that current venture capital schemes in Indonesia are not interested in their (SME) export plans. The association has good experiences with freight forwarders that are willing to accept small amounts for exports.

3.2 SME exports through trade networks

3.2.1 Trading House: Key access for SME to international markets

A trading house (TH) is basically an intermediary in trading activities for goods and services, mainly linking suppliers cum exporters to offshore buyers. There are three types of activities of a TH, i.e., (i) selling local products in the international market; (ii) selling international products in the local markets; and (iii) trading products in the international market.

A study by CESS, Swisscontact and TAF in 2000 and 2001 in Jepara, Yogyakarta and Bali showed that Trading Houses play an important role as provider of Business Development Services and financial services to SMEs in the field: Generally all Trading Houses provided support to SME in the field of:

- (i) provision of working capital through down payment (DP);
- provision of raw/supporting materials;
- (iii) production technology improvement;
- (iv) product development;
(v) improvement of managerial capacities;
(vi) fair trading;
(vii) market expansion.

By providing such a wide range of services, Trading Houses play an important role in facilitating indirect export of SME and SME exporters cooperating with TH show remarkable economic performance. SMEs achieved an average net profit rate of 11% p.a. for wooden furniture in Jepara for the last seven years; (ii) for the handicraft sector in Yogyakarta an average profit rate of 21.3% p.a. for the last nine years; and (iii) for the handicraft sector in Balinan average profit rate of 33.9% p.a. for the last 4 years.

Due to the tense competition in furniture and handicraft sector it was difficult for producers to raise prices. The main source of improved profits was derived from an increase in production and sales turnover with market expansion, which was supported by:

- the increased number of THs pushed demand, resulting in business expansion, sales volume and export value (Jepara and Yogyakarta) for SME producers;
- increased options for SME to choose / select THs which could best serve SME based on criteria (a) price offered by the TH in line with demand of product quality resulting in sufficient profit margins for SME; (b) mode of payments enabling SME obtain working capital/financial liquidity to improve production; (c) no bad track record in payments; and (d) TH strict adherence to quality specifications. By cooperating with several THs, SME could sell reject products to other THs with lower quality requirements resulting in savings of repairs; and last
- cooperating with many THs enabled SME to develop products with various designs and improved quality specifications. SME were able to cross-selling quality products among the THs, meaning quality information from one TH could also be sold to another TH with slight modifications in design. These were the main reasons for the market expansion.

**Conclusion:** the policy option for the government to enhance export-oriented SME development is the creation of an enabling environment for business development and trading house growth in the regions for domestic and foreign investments. It is therefore recommended to develop a strong legal foundation for economic actors and streamlining rules and regulations under control of the national government, among others:

1. Defining the legal base clarifying clear contracts among economic actors;
2. Reducing and simplifying business license procedures to setup businesses, and developing a “one-stop-service” for export documentation processing, especially for clusters and export seaports.
3. The local Office of Industry & Trade should issue the Certificate of Origin (CO) prior goods leave the SME premises.
4. Accelerate payments of ‘restitutions of PPN’ and paid at once.
5. Simplifying procedures of processing applications for RPTKA, IKTA letter and KITAS, (Immigration rules for foreigners to work in Indonesia) and Police Permits.
6. Consistency and efficiency in complying with regulations and working permits at the Dept. of Labour and re-entry permits for foreigners at the Ministry of Justice.
7. Streamlining procedures and reducing import duties and taxes for rejected goods.
8. Implementing fair competition policies including monitoring and complaints resolutions.
10. Reducing guarantee bonds when an investor with FDI status intends to setup a Trading House or Confirming House re BKPM Ministry decree No. 38/SK/1999.
3.2.2 Example of business networks for SME export

The following examples illustrate examples of Indonesians intermediaries, supporting direct or indirect SME export.

Indonesia's People's Handicraft Marketing Service (Pekerti Nusantara)

Clusters of both trading and marketing handicrafts as well as provision of business development services (BDS) to SME. BDS include translation services Indonesian – English, business negotiations, information technology, scanning of international market opportunities, and brokering for access to credit. These BDS are offered at reduced fees whenever Pekerti succeeds in obtaining grants from donor agencies. In the future it wants to develop further into a trading house that provide producers with designs that are in high demand internationally. Subsequently, producers are obliged to market the output with new designs through Pekerti for a limited period of time. In due course, it will be in a better position to offer BDS to producers paid out of increased export earnings. Within the framework of becoming a trading house Pekerti scans for orders abroad and collaborates actively with international development agencies to understand which products and designs will be in high demand in the near future. Demand for handicrafts is changing rapidly and small producers are mostly not aware of these quickly changing trends. Pekerti has developed a website and a CD Rom to promote its activities and its products.

The organization is an intermediate for SME exports from some 60 clusters mainly in Java and Bali. In the past it has been working together with more than 100 clusters but it feels that international demand for handicrafts is declining. However, it is also true that in some cases clusters have been able to develop their own marketing channels and they are not longer making use of the services of Pekerti.

Pekerti participates in a limited number of exhibitions and fairs. In the near future it intends to participate in fairs in Frankfurt and Bangkok. Recently, it has visited The Netherlands on the invitation of a Dutch government organization involved in promotion of SME exports from developing countries. Pekerti does not receive support from the Indonesian government to participate in international trade fairs. Occasionally, these costs are paid by donor agencies but most of the times it is the responsibility of Pekerti.

Pekerti has a number of observations with regard to the role of the government in supporting SME exports. First, it is happy with recent simplification of export procedures that facilitate SME exports. It has contributed to a more equal treatment of SME vis-à-vis larger exporters Second, presently, government agencies are very dominant in the selection of trade fairs that will be visited and the choice of SME entrepreneurs that are invited to participate. According to Pekerti it would be better if private sector organizations would play a bigger role as it has better insight into relevant trade fairs than government agencies. The government could play an important role as facilitator. Third, and very importantly, there is at present a lack of a reliable and up to date information center that collects, processes and disseminates information on export opportunities. Present government-run information provision is too broad and, frequently, not sufficiently up to date and, in the case of Pekerti, it has not been a useful tool to penetrate or expand export markets. Moreover, there is no information center that provides information on business opportunities in domestic markets. Pekerti is in favor of the establishment of a center organized on a commercial basis that will primarily serve associations and institutions involved in SME export development.
Small holder Coffee Association (AICE)

The experiences of Pekerti are similar to those of the coffee export association (AICE) in Indonesia. Some 90 percent of the coffee producers in Indonesia are small holders. The association includes 200 members that are presently actively involved in exporting coffee through the association. Presently, most coffee is exported unprocessed. Only some 25 percent of present coffee production is consumed domestically. This percentage has not changed much in recent years in spite of nation–wide advertisement campaigns to promote coffee consumption. It is currently preparing a new advertisement campaign aimed at quality hotels in Indonesia.

One of the main tasks of the association is promoting Indonesian coffee consumption both domestically and abroad. Indonesian coffee exporters face increased competition on international markets from other countries, in particular Vietnam. A main challenge for Indonesian coffee exporters is upgrading of quality to safeguard and expand international market shares.

In the past the Ministry of Agriculture has provided training courses to coffee small holders throughout Indonesia. AICE is of the opinion that these efforts have not been very successful aimed mainly at individual producers and / or regions, and they have not been directed at strengthening the role of the association in Indonesian coffee promotion abroad.

AICE has followed a pro-active approach in addressing the constraints in upgrading production quality and promoting coffee exports from Indonesia. It is setting up a Training Center in Lampung, South Sumatra, which is one of the main coffee producing areas in the country. It has invested some US$ 50,000 in the training facility while it is still in the process to obtaining financial support from international associations. However, it is expected that quality upgrading will boost the sales of Indonesian coffee abroad. This will have a positive impact on the contribution of the members to the association that are partly based on their export sales.

With respect to export marketing AICE is of the opinion that it cannot rely on the market intelligence that is provided by government agencies. It is outdated and not sufficiently accurate to identify export business opportunities. Accurate data on coffee production is of crucial importance to develop marketing strategies. Presently, the statistical information provided by different departments and the Central Bureau of Statistics vary widely which limits the possibilities to forecast coffee production, exports and prices. The association would highly appreciate the development of a sound data-base, based on econometric modeling, that assists in predicting production levels throughout the country. It is willing to pay for such business services.

Mitra Ventura

Mitra Ventura is a semi-government organization that has a mandate to stimulate SME exports. It works closely together with the venture capital scheme Modal Ventura. Mitra Ventura is of the opinion that SME need more than venture capital if they want to participate successfully in export markets. It operates a web portal in collaboration with international partners.

Presently, the company concentrates on business development services for SME furniture and craft exporters. The strategy of the company is that it first needs to convince SME producers that it can contribute positively to their export sales. Subsequently, it has the experience that SME are able and willing to pay for business services. Nowadays, it limits
its provision of services to selected SME clusters in the province of Central Java. Mitra Ventura is of the opinion that BDS is essential also for sustainable participation in export markets as SME producers need to upgrade their technological capabilities continuously to remain competitive. Reference was made to recent problems in the Jepara clusters (Central Java) that are partially caused by poorly managed supply of wood and inexperience in applying adequately to new environmental regulations in Western countries.

According to Mitra Ventura most of the NAFED export international promotion centers have not been very successful in promoting SME exports, mainly because they were not run as businesses but rather as units of departments. In addition, it is of the opinion that NAFED offers a broad range of products and services and, consequently, it lacks specific information, insights on export opportunities and provision of business services that are crucial for successful participation in the export sector.

**Chambers of Commerce and Industry / KADIN and Associations**

Chambers national (KADIN), by law the government partner for business development, is concerned with national policy formulation addressing international bi- and multi-lateral trade agreements. It is mostly concerned with developing policies at national level for its regional chamber and associations’ members.

Regional chambers such as Kadin Jakarta, Kadin West and East Java have programs for SME development in particular for the manufacturing sectors, among others: (i) provision of training in production, design, quality and packaging; (ii) marketing services through websites of the chambers searching for overseas buyers and business matching through individual contacts; (iii) training in IPRs (HAKI), understanding concept and procedures; (iv) assistance in accessing banks and financial institutions for credit schemes; (v) training in export procedures and documentation. Kadin East Java has even a special program to train 50-selected viable SME to become exporters on a cost recovery basis.

Kadin Jakarta is providing marketing services for SME at the Small Industrial Estate (PIK) Pulo Gadung, East Jakarta to promote Indonesian products for exports in cooperation with MOIT – R&D Institutions.

Kadin East Java, Makassar (South Sulawesi) and Manado (North Sulawesi) are also providing marketing services including trade information and business matchmaking for exporters through their websites.
4 GAPS IN CURRENT PROVISION OF SUPPORT AND SERVICES FOR SME EXPORTS

Current government support

Current government support to SME exports is focusing on three main lines of action:

1. Linking and matching international buyers to Indonesian producers through provision of information. Increasingly, use is made of internet services.

2. Promoting the participation of SME in domestic and international trade fairs.

3. Provision of technical support to SME to stimulate their performance on export markets.

Various departments and agencies with much overlap and duplication carry out these activities. There is little coordination. Overlaps and duplication have created inefficiencies and waste of state budgets for similar programs. The Ministry of Industry and Trade, and in particular its agency NAFED, so far, is rated as the best provider of SME export support.

Effectiveness of instruments

This evaluation study leads to the following comments with regard to the effectiveness of the instruments to promote SME exports:

(1) Linking and matching is very important but it requires access to highly up to date information in order to be effective. Present budgets of NAFED and other agencies are not sufficient to purchase or gain access to high quality information. Information is outdated and, consequently, of limited relevance to both buyers and Indonesian producers. It does however provide foreign buyers with general insights on business opportunities in Indonesia and the database is used while preparing trade missions to Indonesia. The Indonesian government is again gradually reopening its international trade promotion centers. Some of them, e.g. in South Africa, are set up as public – private partnerships while others are again fully run by the government.

(2) Review studies show that promoting participation of SME in trade fairs and exhibitions has resulted in some growth of (international) orders for participating SME. However, the review studies also indicate that most of the export growth has not been sustainable, and it has not resulted in a long-term growth of the majority of participating firms. One of the review studies shows that participation in domestic trade fairs was most effective in (temporarily) increasing sales. Government agencies have a decisive role in both the selection of fairs and exhibitions that will be visited and the SME entrepreneurs that will receive sponsorship for participation. In general, there are no invitations for either SME sector associations, intermediaries or trading houses.

(3) Technical support for SME export promotion has been provided most substantially through the NAFED’ export training center (IETC) in Jakarta, which is currently expanding by establishing a number of centers in the provinces. The centers are rated highly and provide professional assistance to SME that want to penetrate or expand in export markets. The main comment from a review study was however that the partly subsidized services of the center are not bundled but aimed at delivering very specific skills and competencies. Consequently, participating in specific training courses only may in many cases be not sufficient given the need for bundled services expressed by many SME. However, bundled services should be provided by intermediaries for selected sector exporters to meet specific buyers demands.
Main gaps

The main gaps in current SME export promotion strategies and activities that we have identified are the following:

(1) There is **no focal point** for up to date information on export opportunities for SME. There are various data sets available through the Internet but some are out of date. The same holds true for information on production, location, and export potentials of Indonesian SME. NAFED is moving in this direction but much can be improved with involvement of the private sector to cover part of the necessary investments. The NAFED website is a guideline to promote Indonesian exports but much more work is expected from SME to search and conclude commercial transactions based on sector and location specifics.

(2) In general, most promotional activities concentrate on specific trade promotion services, while there is only limited attention to the **need for long-term export development**. For example, there appears to be little attention and action among government agencies to assist furniture exporters in clusters such as in Jepara, Central Java, to prepare for ongoing and upcoming changes in international environmental standards (e.g. eco labeling) that will impact the export prospects of the industry. International competitive standards are rising and there is a need to **prepare business for the impact of globalization** on their export business.

(3) The support activities of the various departments and agencies concentrate on promoting and upgrading export capacities of individual firms. There is **no attention for associations, trading houses, or industry clusters** for SME export promotion. Associations and trading houses represent groups of firms or cluster and ensure better chances that support will be sustainable and reach a number of firms simultaneously. Also working through associations and trading houses may be beneficial in gaining access to larger orders with high quality standards that can be executed only by groups or clusters of SME. A focus on associations and trading houses also facilitates the establishment of long-term relationships with buyers that are not solely based on single transactions but **promote long-term business relationships**.

(4) Presently, there is no support to collection and processing of market information by associations and trading houses in spite of the fact that they have good insight into business opportunities abroad. Also a focus on such associations and trading houses would encourage **networking among firms, support joint marketing efforts** and be beneficial for the development of complementary industries.

(5) Current export promotion programs concentrate on Indonesian producers and foreign buyers. Export promotion agencies have so far excluded paying attention to **foreign investment as a strategy** to promote SME in Indonesia in general and exports in particular. Foreign investment is often export-oriented and may include development of SME through subcontracting linkages. This includes both the establishment of foreign firms as well as investment by traders and buyers. The Investment Coordinating Board / BKPM has in its website investors / buyers and Indonesian exporters enquires that could lead to developing linkages and possible investments enhancing Indonesian exports, and to open new export markets and channels to information and technology for SME development.
5 CONCLUSIONS AND RECOMMENDATIONS

The following provides a general conclusion and proposed recommendations over a broad range of promotion efforts for SME exports:

The need for a broader framework

Data suggest that Indonesian SME exports stem from a limited number of sub-sectors and are exported to a limited number of countries. Most governmental promotion efforts have neither resulted in a sustainable long-term increase in SME exports, nor contributed significantly to export diversification. Export promotion has primarily focused on short-term activities geared at individual companies, while neglecting networking among firms, joint marketing efforts, and the potentials of foreign investment to develop export-oriented SME through subcontracting linkage.

Recommendation:

(1) Export promotion should, in line with MoIT's national industrial strategy, be embedded into a wider policy framework of cluster development, investment promotion and R&D support for improving international competitiveness.

(2) The above could be achieved by setting-up National Sectoral Focal Points. These Sectoral Focal Points should co-ordinate stakeholder forums that assess general constraints and elaborate national strategies for addressing the constraints encountered. The stakeholder forums assigned to the Focal Points should include relevant public actors such as Bappenas, MOIT, SMORT, MoF and the Ministry of Communication, as well as relevant business associations.

(3) The policy framework for developing public-private partnership is very important and especially so when developing bottom-up approaches in the process of formulating policies enhancing clustering. The bottom-up industrialization needs two things to occur: (i) the mobilization of unused local resources (financial and human) and (ii) the effective use of these resources. This is where clustering becomes significant because it facilitates specialization and effective investments in small risk-able steps. Local Cluster development is best achieved through 'local leadership groups', which, under private sector leadership will combine relevant public and private sector stakeholders. National policy can support these processes by means of cost-sharing schemes and best practice documentation.

6 For details please refer to ADB TA (Draft) Final Report, recommendations for MTAP, BDS component, point 1.
Streamline national institutions and programs

There is considerable overlap between the export promotion efforts of various ministries and departments. Many public programs appear to have been copied from MOIT and NAFED with regard to both structure and contents. The overlap concerns both export promotion (trade fairs, exhibitions, websites, etc.) and specific trade promotion services to upgrade the capacities of (potential) SME exporters. Overlaps and duplication among line ministries and agencies are creating inefficiencies and wastage of state budgets.

Recommendations:
(4) In order to avoid inefficiencies and budget wastage due to overlaps and duplicating SME export promotion programs, the nearest most logical solution seems to be concentrating all export promotion programs at national level to just one agency, which is NAFED with its supporting IETC and ITPCs. NAFED programs are relatively well rated by the SME producers that have participated in its promotional activities.

(5) In general, the rationale for having three agencies promoting Indonesia overseas, namely NAFED / ITPC, BKPM (National Investment Coordination Board) and the Tourism Promotion Board, should be reviewed. All three promotion activities are closely linked, with tourism and trade complementing each other and eventually triggering off foreign investment. Case in point is the number of foreigners who originally bought carved wooden furniture in Jepara and afterwards invested into respective manufacturing. With the responsibility for investment permits delegated to Districts/Cities, the role of BKPM in licensing is decreasing. A closer integration of the a/m agencies would facilitate interaction with Indonesian embassies abroad, as well as reduce overlap in promotion activities, such as NAFFED and BKPM running similar match-and-link services on their respective homepages.

Enhance interaction with business associations and the private sector

Linking and matching is very important but it requires access to highly up to date information in order to be effective. Present budgets of NAFED and other agencies are not sufficient to purchase or gain access to high quality information. Information is outdated and, consequently, of limited relevance to both buyers and Indonesian producers. Presently, there is no support to collection and processing of market information by associations and trading houses in spite of the fact that they have good insight into business opportunities abroad.

Recommendations:
(6) Close the information gap by promoting public-private partnership in information generation and dissemination. This could be most probably achieved by establishing the (proposed) SME Portal at national level, established by the SBC and managed by NAFED and private partnerships for professional content and special market intelligence and opportunities on a partial cost recovery basis.

(7) In order to strengthen the capabilities of business associations in collection and dissemination of market intelligence, it is proposed to set up a cost-sharing (matching grant) scheme for first-time market research of business associations. Eligibility for this cost-sharing scheme should be linked to the respective association presenting a feasible concept for dissemination of the market intelligence generated to members and the interested public.
(8) Within the general process of streamlining government institutions and programs, the various governmental websites (MOIT/NAFED, BKPM, but none of MOCSME) should be consolidated and refocused onto provision of information on governmental activities, including legal issues, export and customs procedures, support programs and information on trade fairs, exhibitions and similar events. Match and link activities should be left to business associations and the private sector. Government websites should include links to respective website content.

Review specific support programs

NAFED programs are relatively well rated by the SME producers that have participated in its promotional activities. Its outreach is however limited and annually only a few hundred producers receive NAFED support. Interestingly, a survey among SME producers suggests that participation in domestic trade fairs contributed most to increased sales compared to joining international trade fairs.

Recommendations:

(9) In order to expand outreach of export training, it is suggested for NAFED to adopt a facilitating approach. Export training should be primarily delivered through business organizations and chambers of commerce. Within this set-up, NAFED’s primary roles would be (i) maintaining a data base of accredited, qualified lecturers and trainers, (ii) developing training concepts, curricula and manuals, and (iii) assisting business organizations in organizing and delivering export training at cost-covering fees. The close interaction between NAFED and business associations brought about by such a facilitating approach is also expected to enhance NAFED’s knowledge of sector-specific constraints and opportunities.

(10) What concerns government support to SME trade fair participation, it is recommended to sharpen eligibility criteria and place higher relevance on domestic trade fairs. Government support should be restricted to ‘new-comers’, i.e. SME intending to participate for the first time in a specific trade fair. In order to restrict failure risks, participation in foreign trade fairs should only be supported if SME have already successfully participated in domestic trade fairs and demonstrate the potential to be able to satisfy recurring export orders.

(11) As sector focus and target markets vary strongly among Indonesian provinces, on a medium-term perspective, a stronger role of the provinces in export promotion activities should be envisaged. NAFED’s role in such a decentralized set-up would be twofold: (i) Providing specific expertise and assistance to provinces interested in starting their own promotional activities, and (ii) promoting, by provision of information on markets and relevant events, development of domestic trade, in particular between Java and outer islands. Domestic trade promotion may include financial support to district and province governments in peripheral areas for promoting local produce in Indonesia’s main population and business centers.