

# **Energy in the Japan-Indonesia Economic Partnership Agreement**

Influence Over Action



Friday August 28<sup>th</sup>, 2009

**Michael Boyd**  
**Johns Hopkins University**  
**School of Advanced International Studies**

# Agenda

## ➤ Background

- Diplomatic and Economic Relations
- Energy Relations

## ➤ Japan-Indonesia Economic Partnership Agreement (JIEPA)

- Background and Purpose
  - ◇ Japan
  - ◇ Indonesia
- Negotiations
- Provisions
  - ◇ General
  - ◇ Energy-specific

## ➤ Results with Respect to Energy

- Direct/Short term
- Indirect/Long term

## ➤ Lessons Learned

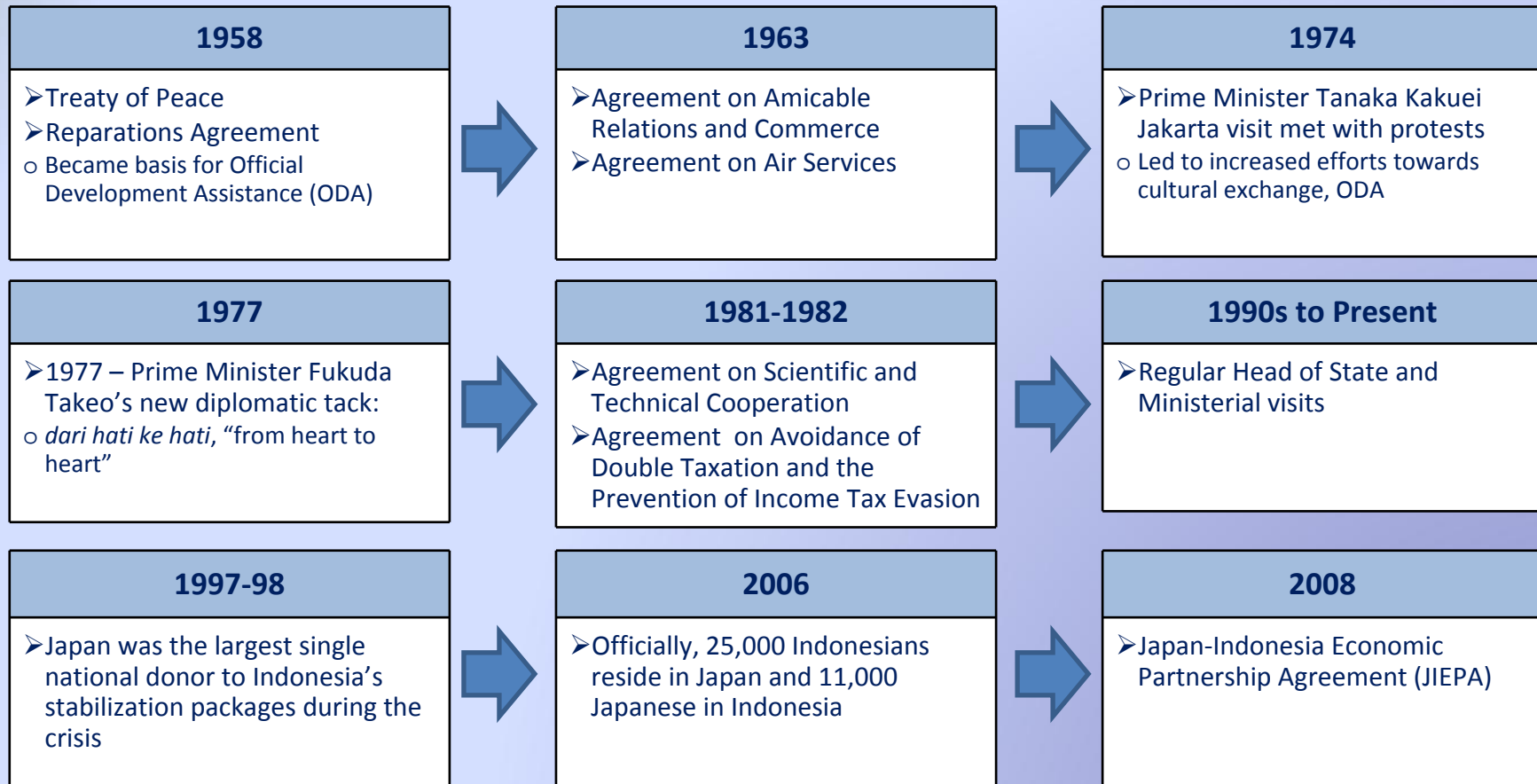
- Focus: Energy Supply Guarantee

## ➤ Conclusion & Implications

- The Pitfalls of International Agreements

# While tense at times, Japan-Indonesia bilateral diplomatic relations have generally been mutually beneficial

## Major treaties, cooperation, and diplomatic events



## The bilateral trade relationship is important for both parties, but to different degrees

For Indonesia, Japan is its largest trading partner

### Indonesia trade by main destination, % share

<u>Exports</u>					
<u>2006</u>		<u>2007</u>		<u>2008</u>	
Japan	21.6	Japan	20.7	Japan	20.7
EU	12.0	EU	11.7	EU	11.6
US	11.2	US	10.2	US	9.8
<u>Imports</u>					
<u>2006</u>		<u>2007</u>		<u>2008</u>	
Singapore	16.4	Singapore	13.2	Singapore	17.2
China	10.9	China	11.5	China	12.1
EU	9.9	EU	10.3	Japan	12.0

- Japan is also a major destination for Indonesia's non-energy exports, receiving **17%** of the 2007 total
- Indonesian exports to Japan of manufactured and other higher-valued added goods are much smaller by value
- Trade balance averages 3:1 or 4:1 in Indonesia's favor

For Japan, Indonesia is less important overall, but crucial in key areas

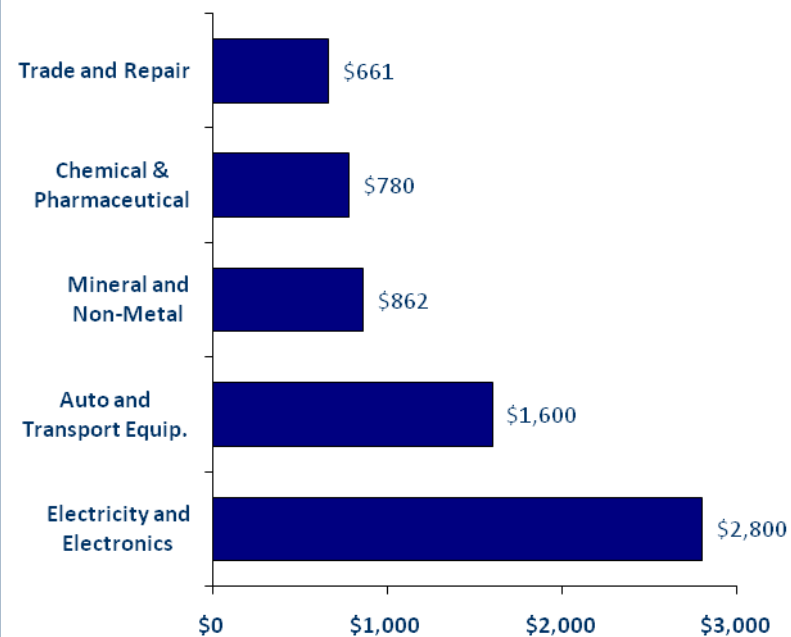
### Japan trade by main destination, % share

<u>Exports</u>					
<u>2006</u>		<u>2007</u>		<u>2008</u>	
US	22.5	US	20.1	US	17.6
EU	14.5	China	15.3	China	16.0
China	14.3	EU	14.8	EU	14.1
<u>Imports</u>					
<u>2006</u>		<u>2007</u>		<u>2008</u>	
China	20.5	China	20.6	China	18.8
US	11.8	US	11.4	US	10.2
EU	10.3	EU	10.5	EU	9.3

- Indonesia consistently ranks in the mid-teens and mid-single digits in export and import share, respectively
- But since the 1970s, Japan has been the major destination Indonesia's fuel, metal, and mineral exports

# Japan has more cumulative investment in Indonesia than in any other SE Asian country

## Realized Japanese non-oil and gas investment (2007), mil.USD



## Employment

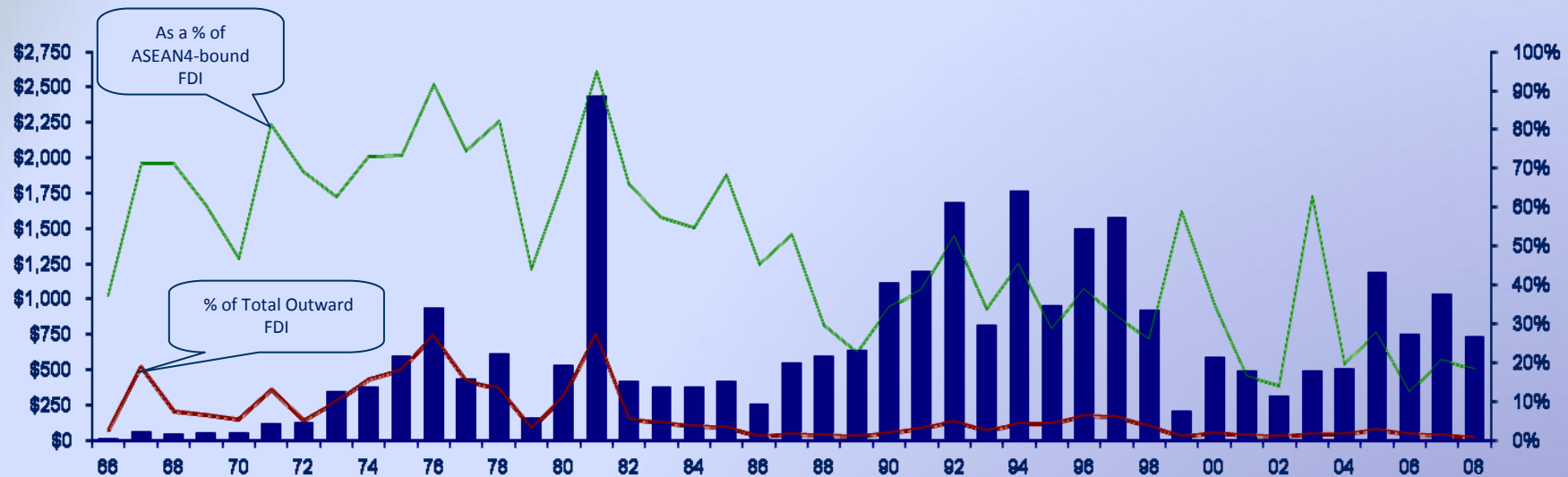
➤ As of 2006, there were approximately 1,000 firms employing approximately 280,000 local staff

## Lending and finance

➤ Japan is also Indonesia's largest creditor, with more than \$20.0 billion outstanding

# Despite the robust long term economic relationship, since the 1997-98 Financial Crisis investment declined significantly

Annual Indonesia-bound Japanese investment, MMUSD



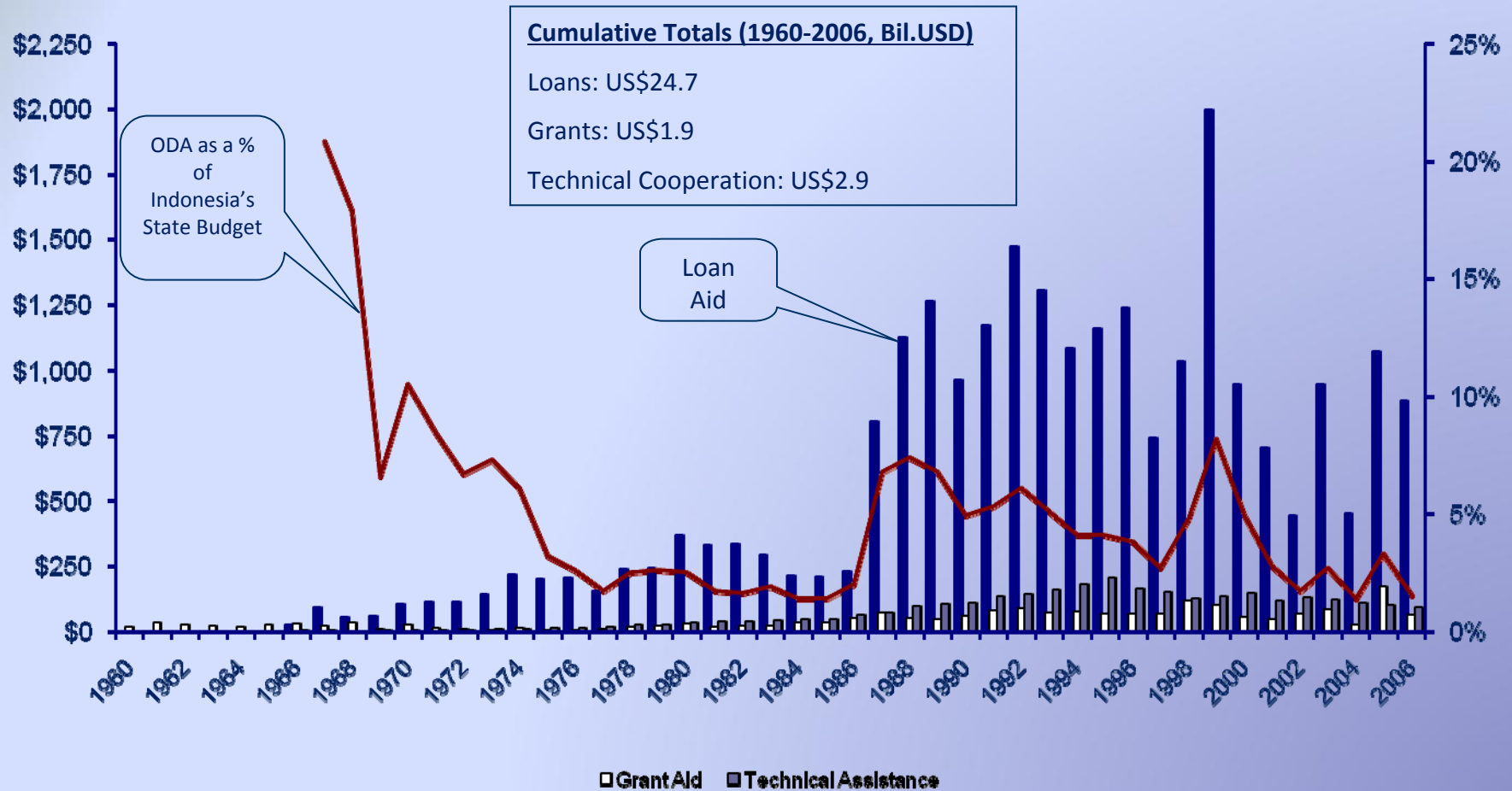
Indonesia-bound investment by source country, ranking (MM USD)

1966-1998	2000-2008	2006	2007	2008
Japan was the #1 investor with a cumulative \$24.6 billion	1. EU \$6,224 2. USA \$1,833 3. Japan \$1,612 4. China \$1,210	1. EU \$1,995 2. Japan \$1,059 3. Australia \$366 4. Korea \$317	1. EU \$2,409 2. Japan \$1,125 3. US \$1,093 4. Australia \$309	1. Japan \$1,518 2. EU \$1,063 3. US \$873 4. Australia \$390

Notes: ASEAN4 refers to Indonesia, Malaysia, Philippines, and Thailand. Series discontinuity at 1995: pre-1995 data based on reports and notifications, post-1995 are BoP-basis, net and flow  
Source: JETRO, BKPM, US Embassy in Jakarta, BKPI, ASEAN Statistical Yearbook 2008

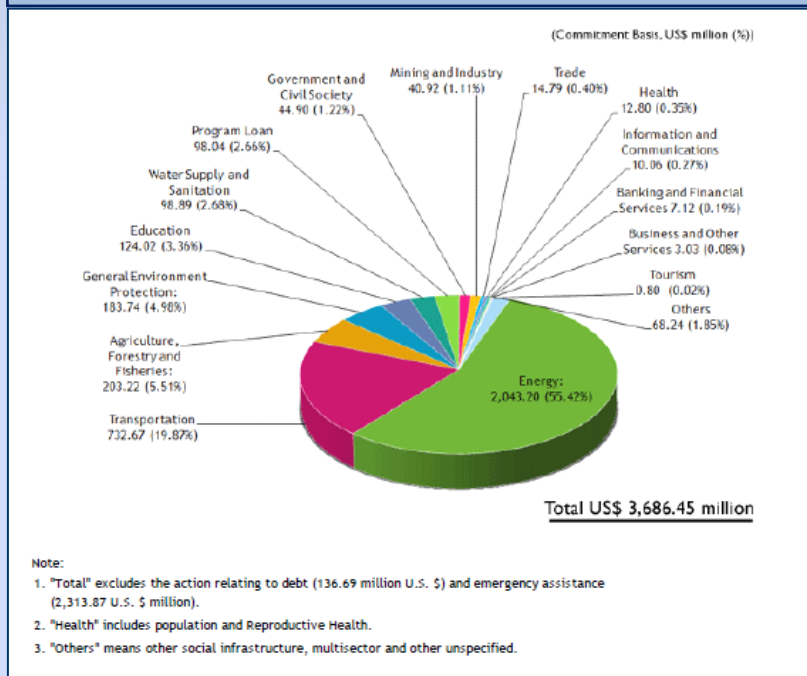
# Japan is Indonesia's largest cumulative ODA donor, although the amounts have declined in recent years

Japan's ODA to Indonesia 1960-2006, Bil.USD, % of State Budget



# Japan's ODA has focused on infrastructure and energy, and has made large contributions on a percentage basis

## Japan's ODA to Indonesia by Sector ('03-'05)



## Japan's ODA to Indonesia Provided:

- Electric power: 20% overall capacity of electrical power
- Roads : approximately 20% of the expressways in the Jakarta Metropolitan Area
- Communications: approximately 50% of the construction of the communications network
- Railways: 50% of the restoration of the Java Main Line
- Dams: 30% of the country's dams (approximately 55% of total effective reservoir capacity)
- Health care : two of the four A-Class core public hospitals
- Education: constructed 600 schools in 12 states Nationwide (Yen loan)

Note: all figures approximate

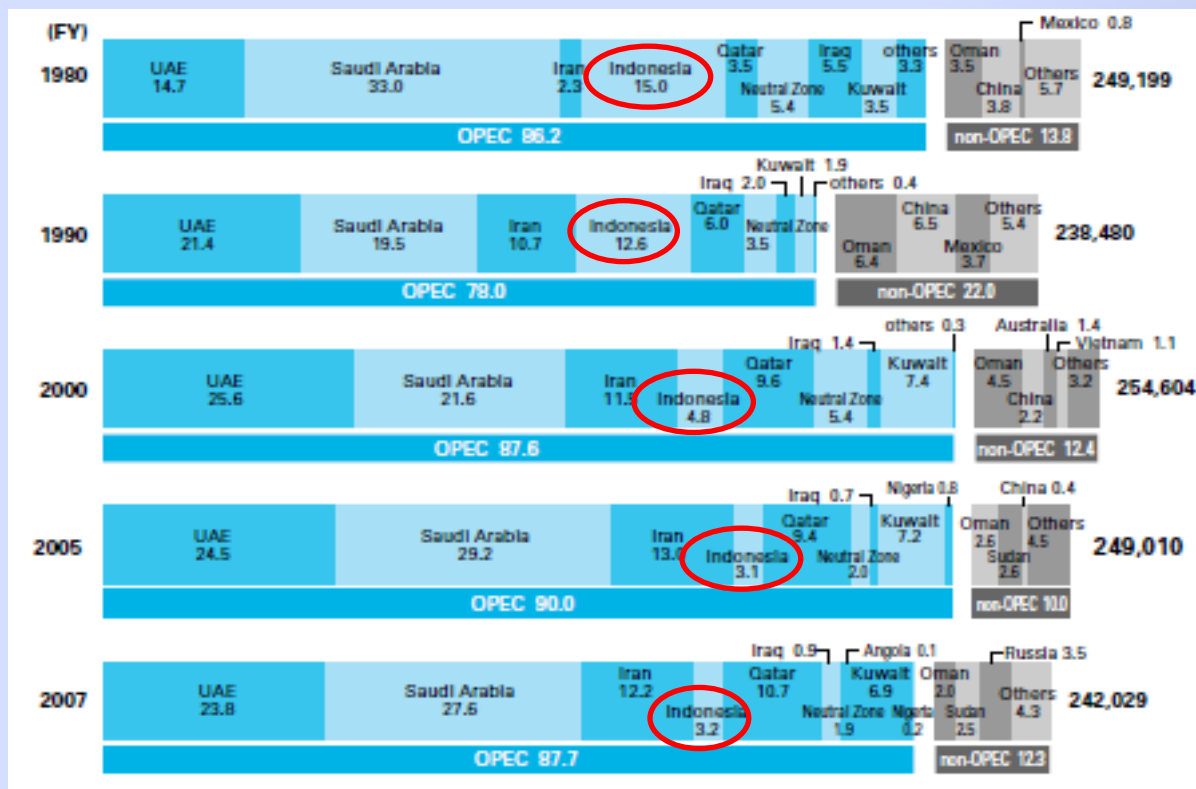


# Agenda

- Background
  - Diplomatic and Economic Relations
  - Energy Relations
- Japan-Indonesia Economic Partnership Agreement (JIEPA)
  - Background and Purpose
    - ✧ Japan
    - ✧ Indonesia
  - Negotiations
  - Provisions
    - ✧ General
    - ✧ Energy-specific
- Results with Respect to Energy
  - Direct/Short term
  - Indirect/Long term
- Lessons Learned
  - Focus: Energy Supply Guarantee
- Conclusion & Implications
  - The Pitfalls of International Agreements

# Indonesia has declined in importance as an oil supplier to Japan (and the rest of the world)

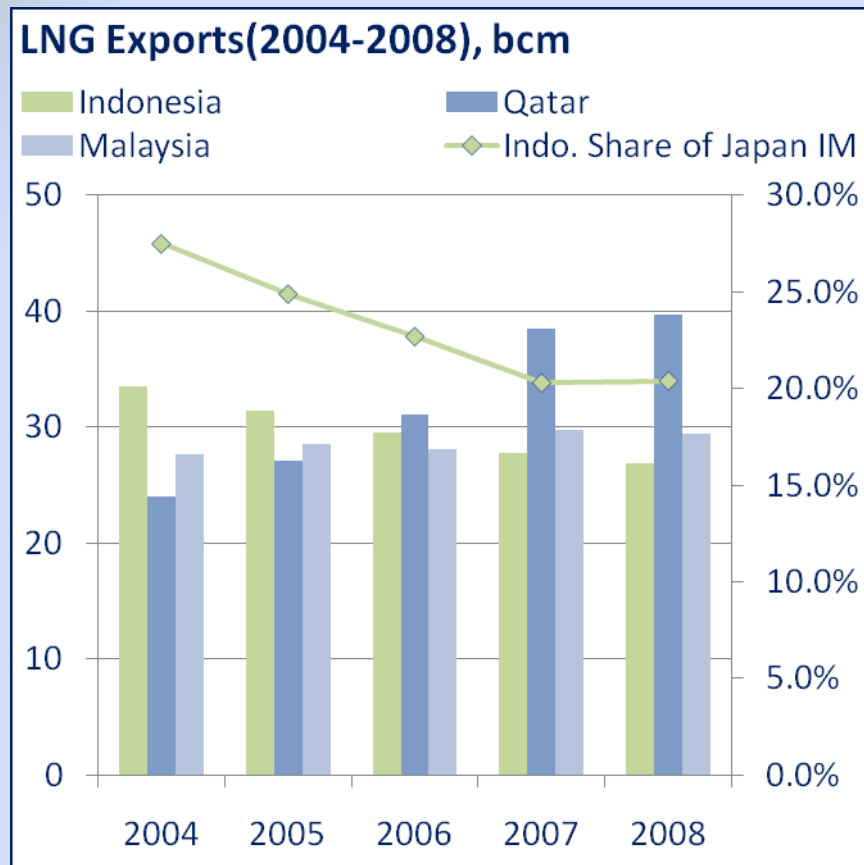
Japan crude oil imports by source, '000kl, %



**Indonesia is now a net crude importer and no longer a member of OPEC**

# The bilateral energy relationship has traditionally been very close in LNG, wherein Japan is the world's largest buyer

Indonesia was until 2005 the world's largest LNG supplier



## Japanese investment drove development of Indonesia's LNG sector

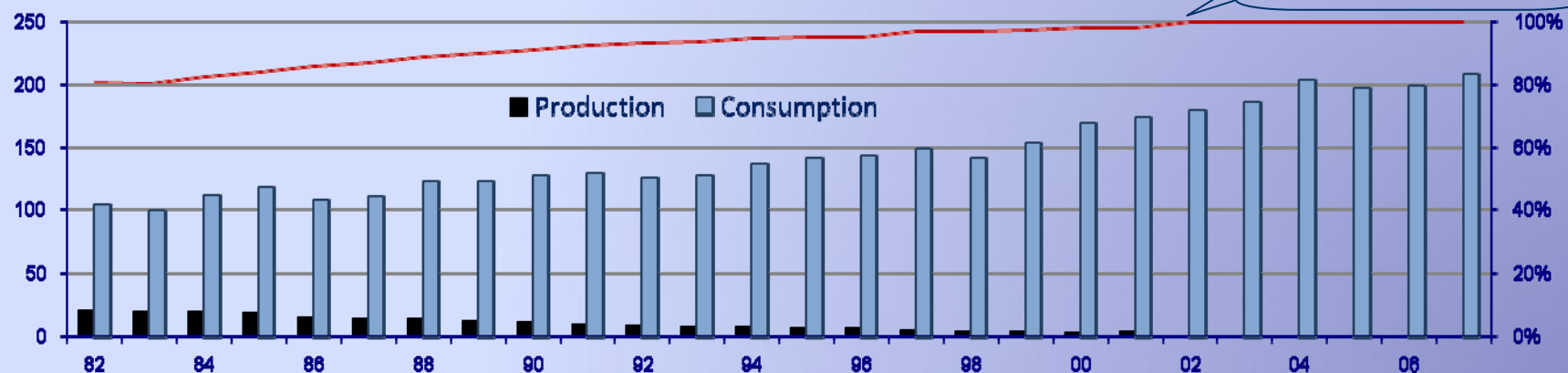
- Both of Indonesia's first two LNG liquefactions plants (Arun, Bontang) were initially developed in the 1970s under long term contract with Japanese firms
  - Excess supply was allocated to other buyers
- Indonesia's third LNG plant (Tangguh) is being developed by a BP-led consortium that includes Japanese firms
  - Exports are more widely diversified, with shipments going to Korea, China, the US and Japan
- Thru 2007, Japan purchased 70% of Indonesia's LNG cumulative LNG exports

# Japan is Indonesia's largest coal export destination, and Indonesia is Japan's second-largest source of imports

Indonesia's Major Coal Export Destinations, '000 tons

Country	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009*
Japan	13,177	15,216	16,560	17,992	19,013	24,237	23,128	25,234	26,879	17,836
Taiwan	13,520	11,507	13,100	14,144	16,678	14,524	17,070	18,670	14,833	12,256
Korea	4,779	5,552	5,633	6,966	9,690	9,964	10,925	13,765	14,836	12,931
Hong Kong	2,914	4,662	5,564	9,178	8,230	8,970	9,373	12,079	10,936	6,626
India	3,151	3,130	4,586	6,700	5,465	8,740	10,846	14,227	14,683	15,088
Thailand	2,564	2,318	3,155	4,075	2,217	4,256	4,298	5,841	8,429	5,210
Malaysia	2,761	2,098	6,239	3,823	4,315	4,028	5,293	6,234	7,107	4,866
Other	15,504	20,798	18,729	22,802	28,151	36,071	62,700	43,998	42,816	32,700
<b>Total</b>	<b>58,460</b>	<b>65,281</b>	<b>73,563</b>	<b>85,680</b>	<b>93,759</b>	<b>110,790</b>	<b>143,633</b>	<b>140,048</b>	<b>140,519</b>	<b>107,513</b>

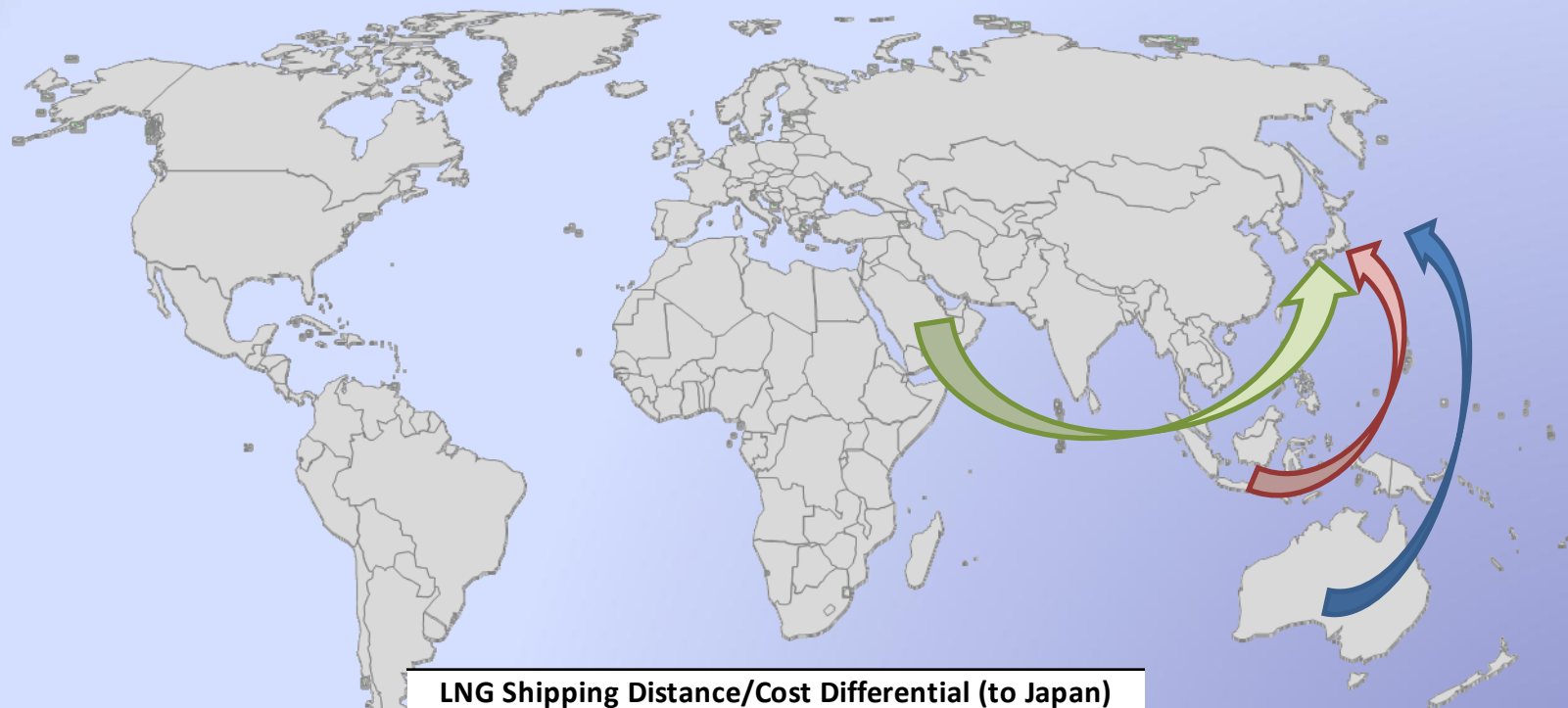
Japan's Coal Production & Consumption (1981-2008), MM Short Tons



\* Through September 2009

Source: Ministry of Energy and Mineral Resources, IEA, ESDM Datawarehouse

## Indonesia is significantly less distant than the Middle East, and subject to an independent political cycle



<b>LNG Shipping Distance/Cost Differential (to Japan)</b>			
<b>Distance (Nautical Miles)</b>		<b>Delivered Cost (\$/MMBtu)</b>	
Borneo	2660	Borneo	0.51
Australia	3680	Australia	0.59
Middle East	6500	Middle East	0.96

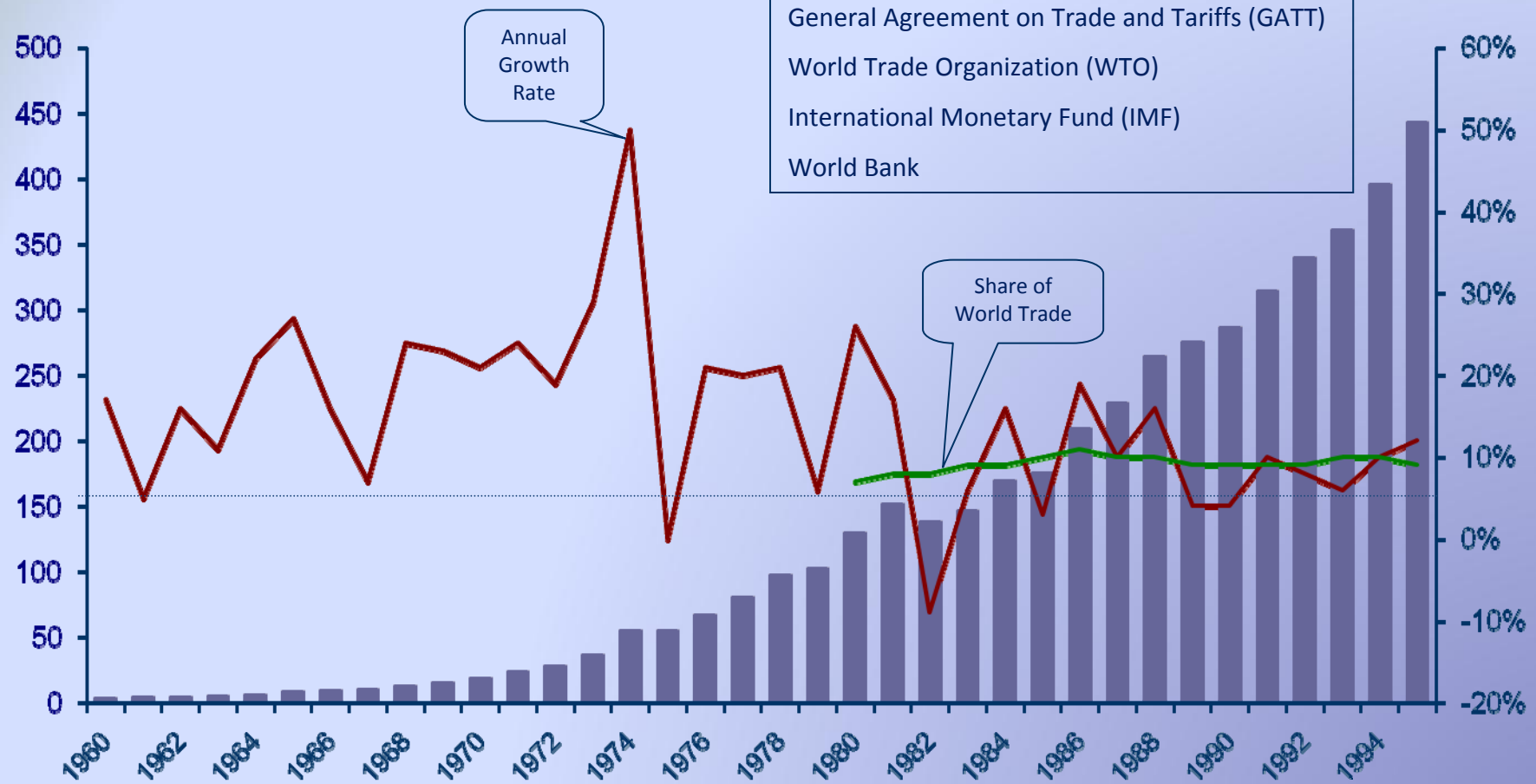
Note: Delivered cost is calculated assuming 165,500 cubic meter membrane vessel at T/C \$75,000 per day  
 Source: Poten & Partners

# Agenda

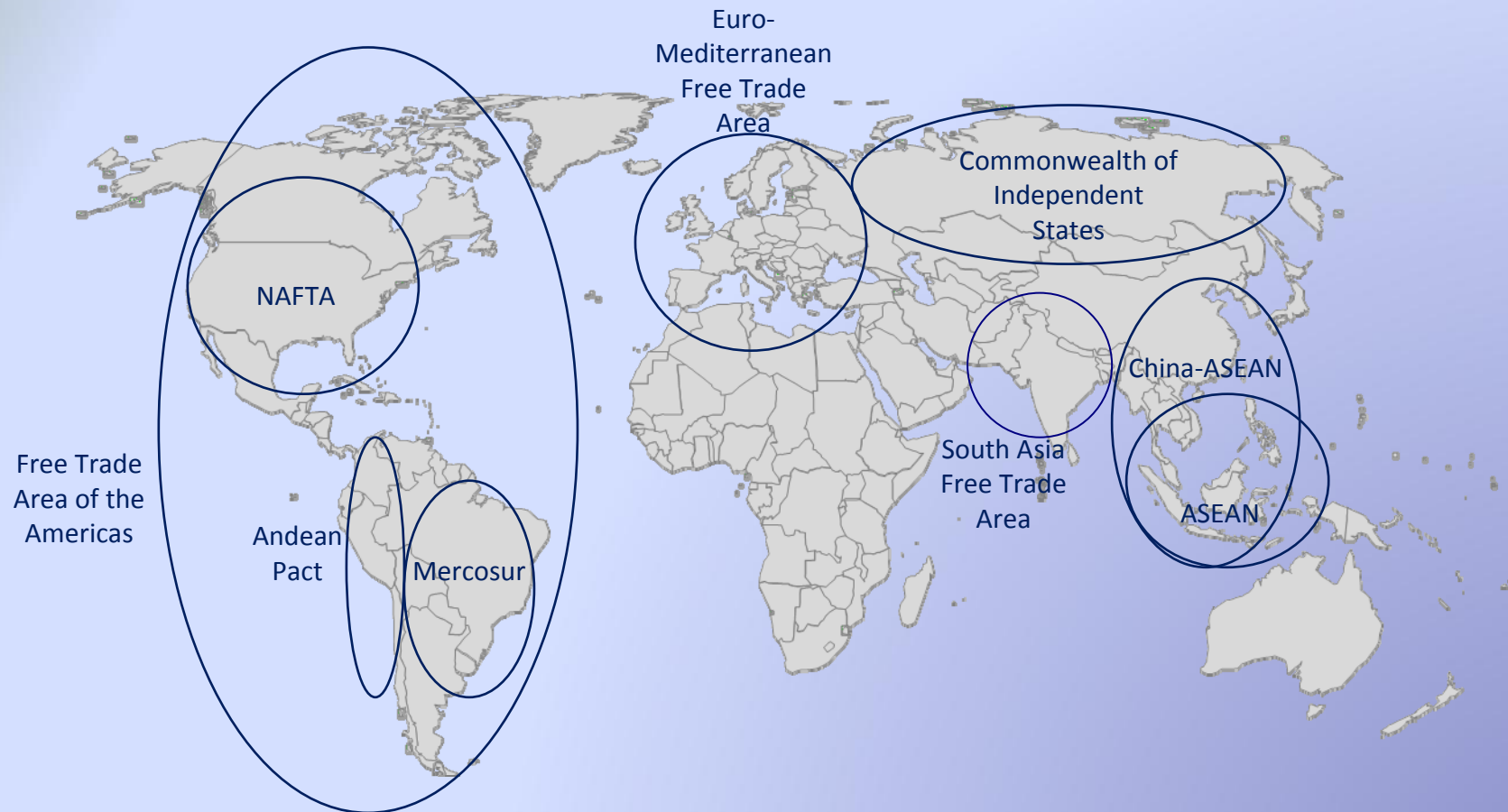
- Background
  - Diplomatic and Economic Relations
  - Energy Relations
- Japan-Indonesia Economic Partnership Agreement (JIEPA)
  - Background and Purpose
    - ◇ Japan
    - ◇ Indonesia
  - Negotiations
  - Provisions
    - ◇ General
    - ◇ Energy-specific
- Results with Respect to Energy
  - Direct/Short term
  - Indirect/Long term
- Lessons Learned
  - Focus: Energy Supply Guarantee
- Conclusion & Implications
  - The Pitfalls of International Agreements

# Until the mid-1990s Japan relied on multilateral arrangements to open overseas markets

Total Japanese exports, Bil.USD

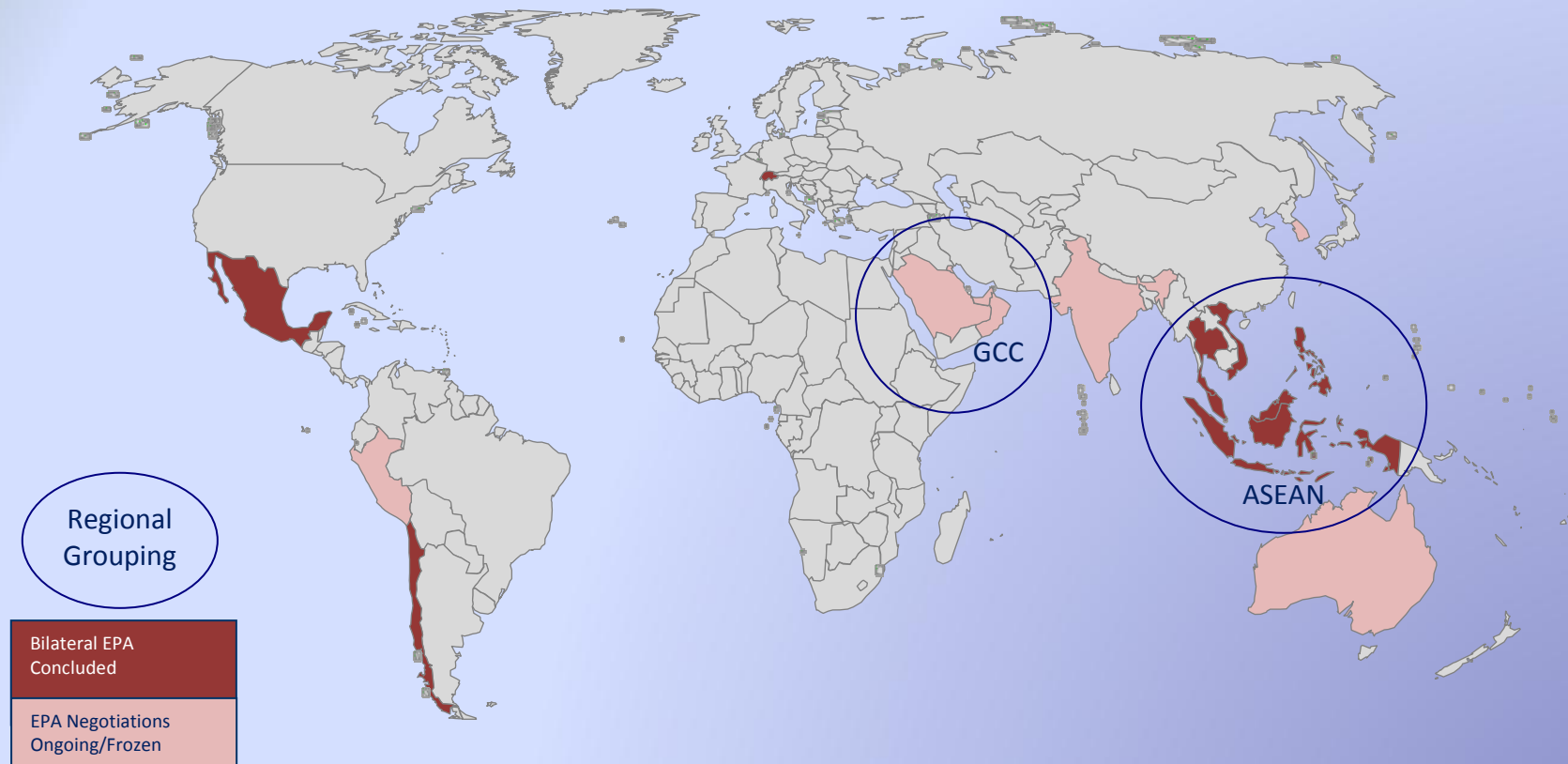


# But it gradually became clear that Japan would have to act bilaterally and regionally in order to not be left behind





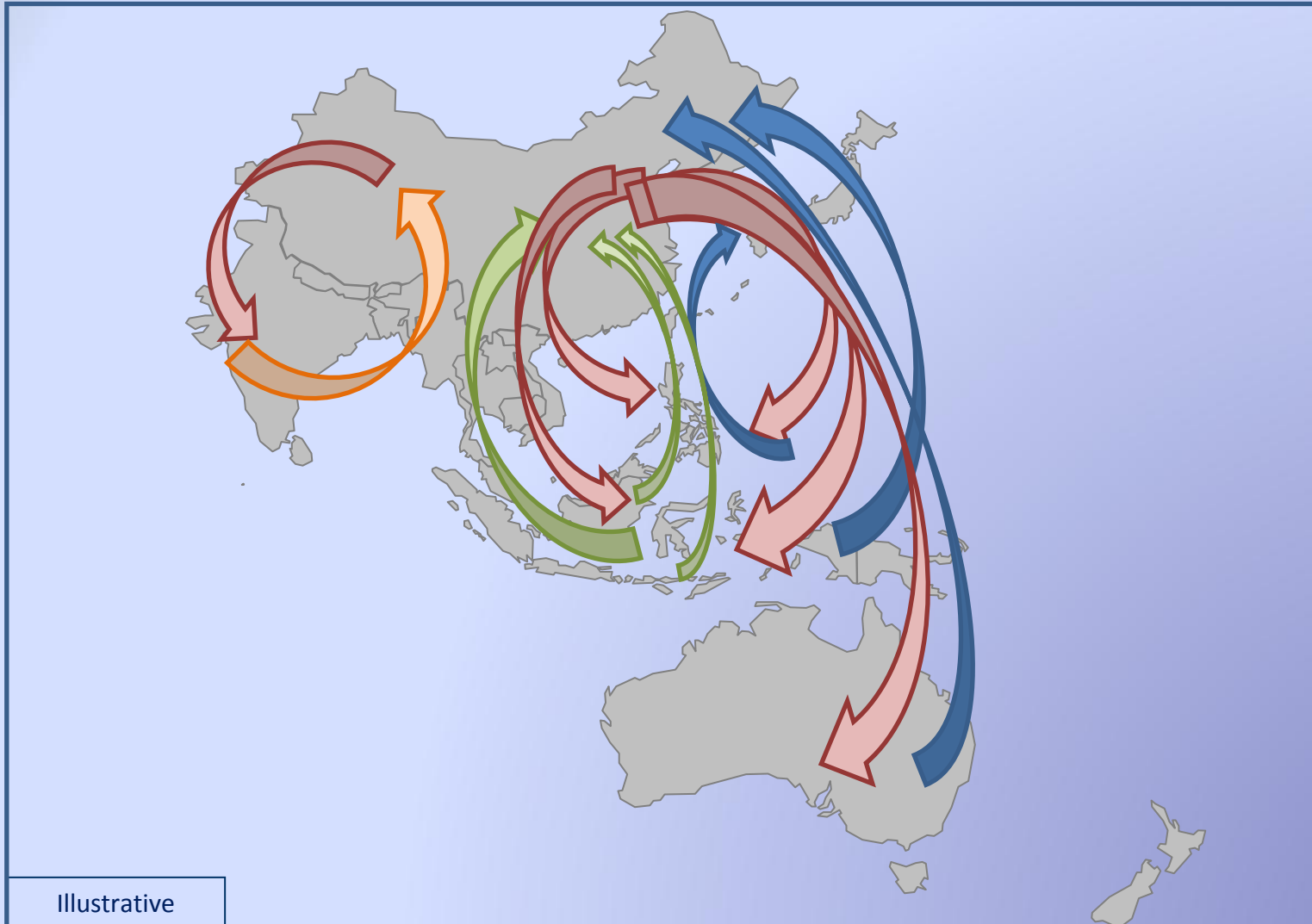
# And act it has, aggressively negotiating and signing EPAs with regional and extra-regional partners



Note: As of August 2009

Source: Ministry of Foreign Affairs of Japan

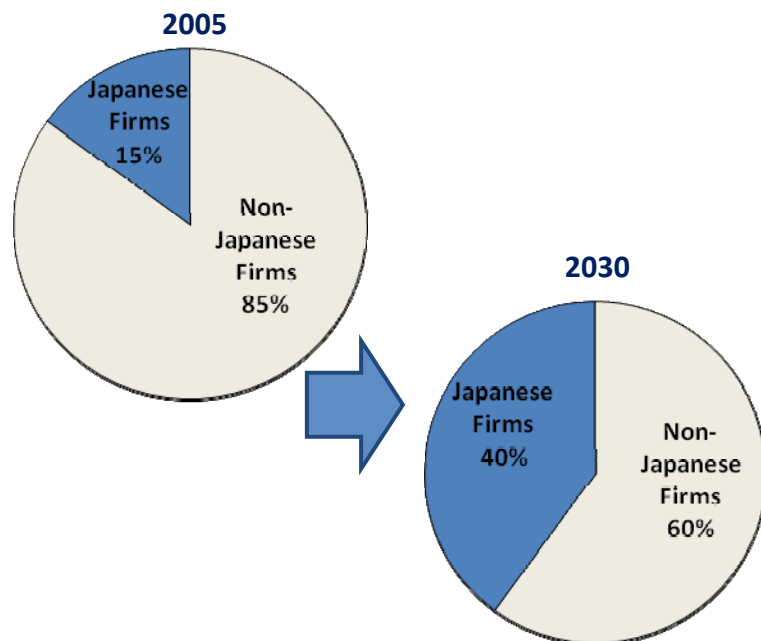
**From a geopolitical perspective, from the late 1990s onward  
China's presence was increasingly felt across the region**



## In JIEPA, Japan sought improved security of energy supply, business environment, and trade/investment opportunities

### Increased Security of Energy Supply

Share of imported oil produced by:



### Other Goals

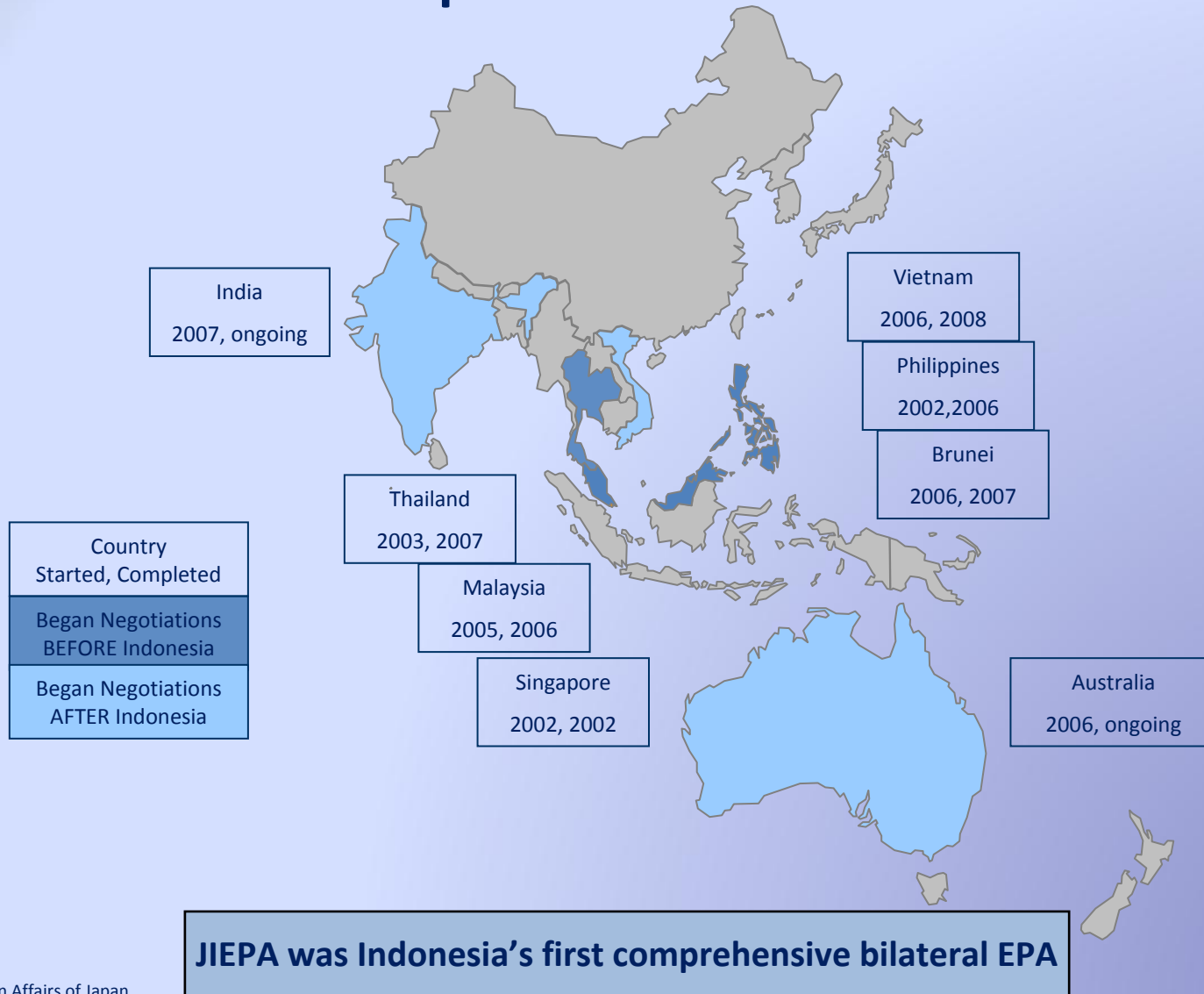
- Increased trade and investment opportunities
  - Market Access
    - Tariff reduction
  - Customs and import procedure simplification and clarification
  - Duty-free import of highly specialized materials for use in manufacturing
- Improved business environment in Indonesia
  - Reinforced sanctity of contracts and dispute resolution mechanisms

**JIEPA was partially an attempt to revive the broader energy relationship**

# Agenda

- Background
  - Diplomatic and Economic Relations
  - Energy Relations
- Japan-Indonesia Economic Partnership Agreement (JIEPA)
  - Background and Purpose
    - ◇ Japan
    - ◇ Indonesia
  - Negotiations
  - Provisions
    - ◇ General
    - ◇ Energy-specific
- Results with Respect to Energy
  - Direct/Short term
  - Indirect/Long term
- Lessons Learned
  - Focus: Energy Supply Guarantee
- Conclusion & Implications
  - The Pitfalls of International Agreements

# Indonesia also needed to keep up with its competitors' EPA/FTA efforts with Japan



# In JIEPA, Indonesia sought improved market access, investment, capacity-building, and movement of persons

## The Three Pillars of the Japan-Indonesia Economic Partnership Agreement

### I. Trade and Investment Facilitation

- In order to:
  - Increase investment across the Indonesian economy from its largest cumulative investor
- Measures include:
  - Improve Indonesia's investment climate and build Japanese investors' confidence
  - Customs procedures
  - Port Services
  - Standards

### II. Liberalization

- In order to:
  - Increase trade with its largest trade partner
- Measures include:
  - Reduce or remove tariff and non-tariff barriers to trade
  - Export of semi-skilled labor
    - Nurses and caregivers

### III. Cooperation

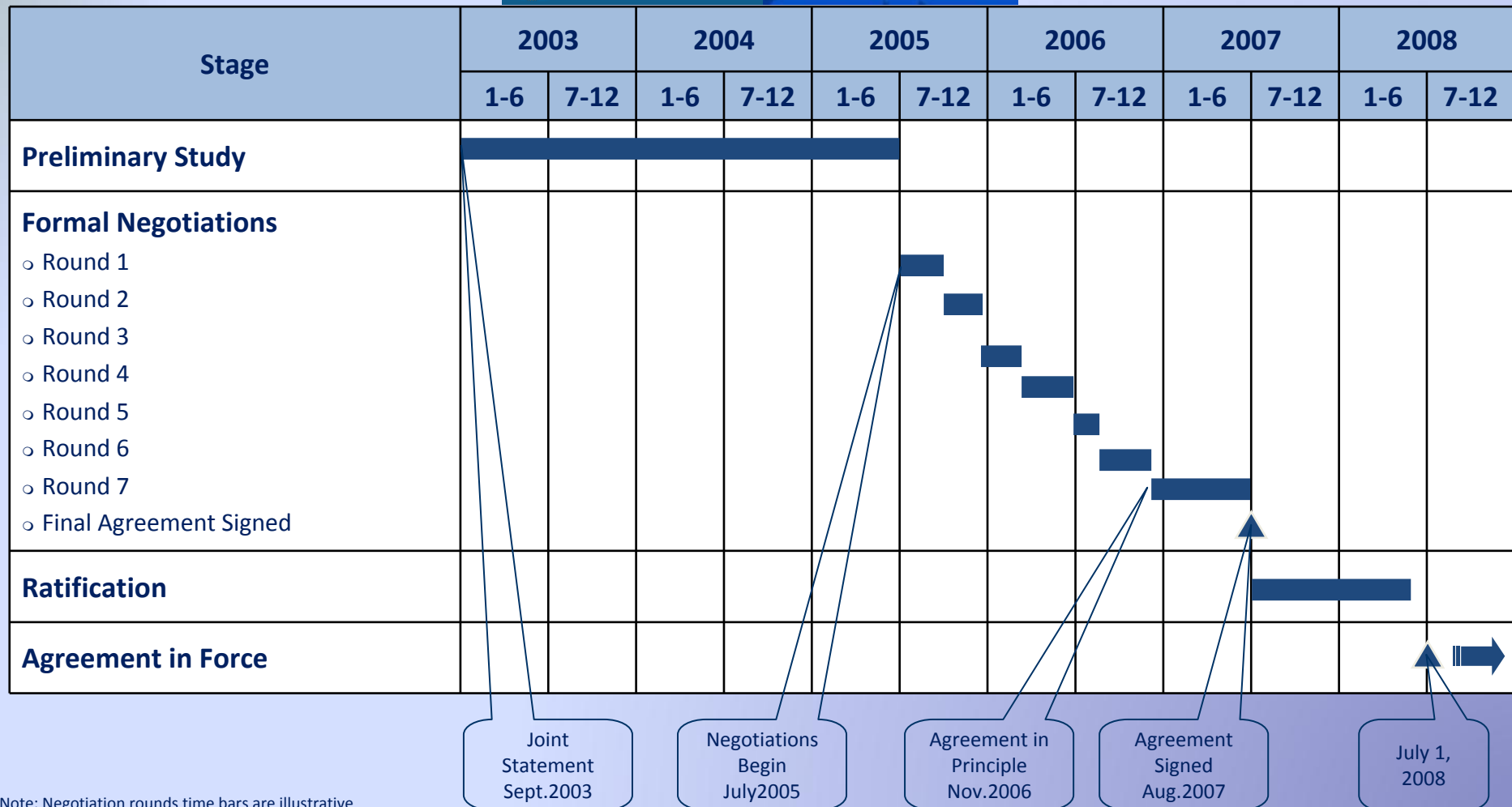
- In order to:
  - Move up the development ladder to higher-value activities
- Measures include:
  - Capacity building
  - Technology transfer
  - Technical assistance to specific industries
    - Manufacturing Industry Development Center



# Agenda

- Background
  - Diplomatic and Economic Relations
  - Energy Relations
- Japan-Indonesia Economic Partnership Agreement (JIEPA)
  - Background and Purpose
    - ✧ Japan
    - ✧ Indonesia
  - Negotiations
  - Provisions
    - ✧ General
    - ✧ Energy-specific
- Results with Respect to Energy
  - Direct/Short term
  - Indirect/Long term
- Lessons Learned
  - Focus: Energy Supply Guarantee
- Conclusion & Implications
  - The Pitfalls of International Agreements

# While originally envisioned to require perhaps a year, in the event JIEPA negotiations took nearly three years



Note: Negotiation rounds time bars are illustrative

Source: Ministry of Foreign Affairs



## Why did it take so long? Sticking points included:

### Japan

- Market Access
  - Agricultural market



- Labor Market



### Indonesia

- Policy coordination among Ministries
  - Indonesia's first bilateral, comprehensive EPA



- Market Access
  - Tariff reductions on “substantially all” goods (90% of trade by value)

# Agenda

- Background
  - Diplomatic and Economic Relations
  - Energy Relations
- Japan-Indonesia Economic Partnership Agreement (JIEPA)
  - Background and Purpose
    - ◇ Japan
    - ◇ Indonesia
  - Negotiations
  - Provisions
    - ◇ General
    - ◇ Energy-specific
- Results with Respect to Energy
  - Direct/Short term
  - Indirect/Long term
- Lessons Learned
  - Focus: Energy Supply Guarantee
- Conclusion & Implications
  - The Pitfalls of International Agreements

## JIEPA is truly comprehensive, with thirteen chapters covering many and varied areas

Chapter	Description
<b>1. Trade in Goods</b>	Agree to eliminate or reduce tariffs comprehensively, in agriculture, forestry, industrial goods
<b>2. Trade in Services</b>	Professional/business, communication, construction, distribution, educational, financial, health related and social, tourism and travel related, transport services
<b>3. Customs Procedures</b>	Promote information exchange and cooperation, simplification and harmonization of customs procedures, and ensuring effective enforcement
<b>4. Investment</b>	Provide a framework for further expansion and facilitation of cross-border investment
<b>5. Movement of Natural Persons</b>	Provide a framework for facilitating movement of natural persons including short-term business visitors, intra-corporate transferees, investors and professional services. Establish a scheme of acceptance for <u>nurses and care-workers</u> Consider widening the scope of "the Industrial Training and Technical Internship Program" covering hotel related services.
<b>6. Energy and Minerals</b>	Coordination to promote and facilitate investments in this sector, and to contribute to enhancing security of supply of energy and mineral resources. To this end, both sides will strengthen a policy dialogue and cooperation
<b>7. Intellectual Property Rights</b>	Ensure adequate and effective protection of intellectual property, promote efficiency and transparency in administration of intellectual property protection system, and provide for measures for enforcement of intellectual property rights
<b>8. Government Procurement</b>	Provide a framework for the exchange of information through the contact points and a mechanism for dialogue between the relevant parties
<b>9. Competition</b>	Promote competition by addressing anti-competitive practices and cooperate in strengthening the structure and implementation of such laws
<b>10. Business Environment</b>	Provide a mechanism for improving business environment and business confidence involving government, industry groups, and other interested parties
<b>11. Cooperation</b>	Promote capacity building in manufacturing, agriculture, forestry and fisheries, trade and investment promotion, human resource development, tourism, information technology, financial services, government procurement, and environment

# Agenda

- Background
  - Diplomatic and Economic Relations
  - Energy Relations
- Japan-Indonesia Economic Partnership Agreement (JIEPA)
  - Background and Purpose
    - ◇ Japan
    - ◇ Indonesia
  - Negotiations
  - Provisions
    - ◇ General
    - ◇ Energy-specific
- Results with Respect to Energy
  - Direct/Short term
  - Indirect/Long term
- Lessons Learned
  - Focus: Energy Supply Guarantee
- Conclusion & Implications
  - The Pitfalls of International Agreements

## In a first for a Japanese EPA, JIEPA contains a Chapter focused directly on Energy and Mineral Resources (EMR)

### Key Energy Provisions

Article	Description
<b>98. Promotion and facilitation of investment</b>	Promote and facilitate investment through <u>discussions, exchange of information</u> on laws and regulations, and <u>discussing</u> ways of creating equitable and transparent conditions for investors
<b>99. Import and Export Restrictions</b>	“When introducing a prohibition or restriction [on energy or mineral resource goods]...the Party shall <u>provide relevant information...as early as possible</u> to the other Party and <u>reply to specific questions...with a view to avoiding disruption of ordinary business activities</u> ”
<b>100. Export Licensing Procedures and Administration</b>	The rules for export licensing procedures shall be neutral in application and administered in a fair and equitable manner <u>All rules and procedures shall be published</u>
<b>101. EMR Regulations</b>	EMR agencies should <u>“seek to ensure”</u> that new regulations don’t disrupt existing contracts
<b>102. Environmental</b>	Take into account environmental considerations, encourage environmental technology transfer, promote public awareness
<b>103. Community Development</b>	<u>Welcome</u> community development efforts by investors
<b>104. Cooperation</b>	The Parties shall <u>“endeavor to make available”</u> funds for policy development, capacity building and technology transfer
<b>105. Sub-Committee on Energy and Mineral Resources</b>	Mandates up a permanent consultative body to <u>exchange information and monitor</u> implementation
<b>Annex 12 - Additional Provisions</b>	“Upon request of either Party, the Parties shall <u>consult on risk-sharing measures</u> [JIEPA-speak for infrastructure investment] to support investments by investors of Japan in the energy and mineral resource sector in Indonesia.”

**These provisions are largely notification requirements with no discernable enforcement mechanism**

## There are also a host of JIEPA provisions indirectly-related to energy and parallel energy cooperation initiatives

### Indirectly-related JIEPA provisions

- **Investment:** Provide a framework for further expansion and facilitation of cross-border investment through commitments on:
  - National treatment
  - Most-favored-nation treatment
  - Prohibition of performance requirements
  - Dispute settlement between state and investor
  - Enhanced protection of investors and investment
- **Dispute Resolution:** Details a formal dispute resolution mechanism for disagreements in areas covered by JIEPA
- **Business Environment Enhancement:** Provides another forum for discussion of business environment issues
  - Sub-Committee on Improvement of Business Environment and Promotion of Business Confidence
  - Liaison Office on Improvement of Business Environment

### Separate but parallel cooperation

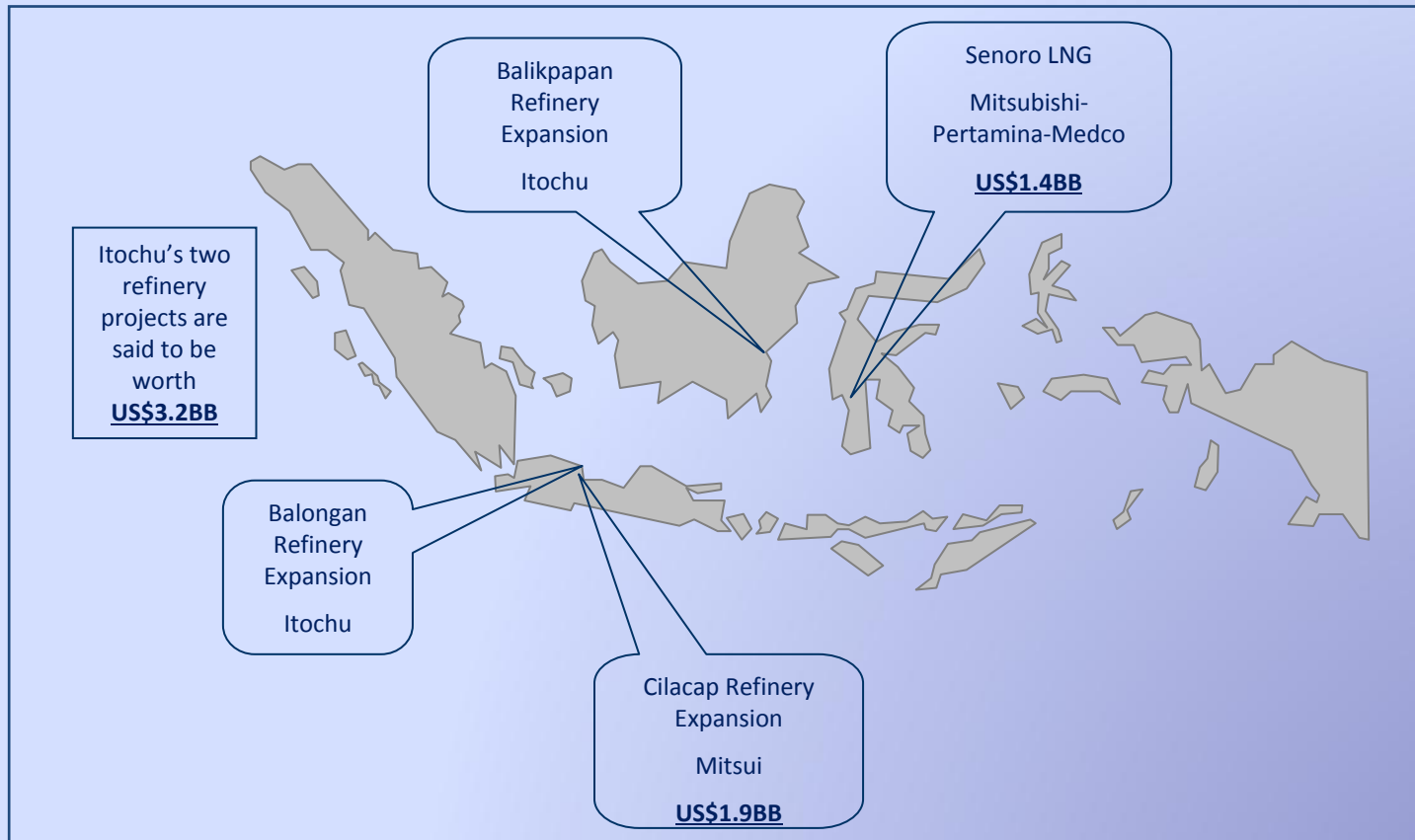
- **Energy Efficiency**
  - JICA-MEMR: Workshop on Energy Conservation Improvement and Efficiency (2007-ongoing)
- **Nuclear**
  - MEXT: Forum for Nuclear Cooperation in Asia (FNCA) [not just Indonesia]
  - Institutional capacity building [bilateral]
- **Bio-fuels**
  - JJC-KADIN: Industrial Joint Forum on Investment's Bio-fuel Sub-Working Group – Industrial Strategy Proposal [Policy Recommendations]
- **Coal**
  - METI-MEMR: Upgraded Brown Coal (UBC) plant in Kalimantan inaugurated Dec.4 2008 (2001-ongoing)
  - Coal to Liquids (CTL): Technological and investment support from Japan to produce 2% of national energy supply by 2025

Cooperation deals were mostly in the works long before JIEPA

# Agenda

- Background
  - Diplomatic and Economic Relations
  - Energy Relations
- Japan-Indonesia Economic Partnership Agreement (JIEPA)
  - Background and Purpose
    - ✧ Japan
    - ✧ Indonesia
  - Negotiations
  - Provisions
    - ✧ General
    - ✧ Energy-specific
- Results with Respect to Energy
  - Direct/Short term
  - Indirect/Long term
- Lessons Learned
  - Focus: Energy Supply Guarantee
- Conclusion & Implications
  - The Pitfalls of International Agreements

## Several billion dollars in energy deals inked on the sidelines of the JIEPA



**But these deals were all in the works long before JIEPA**

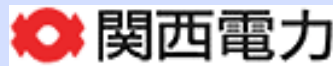
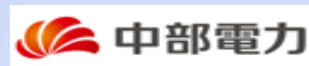


## Because energy supply assurances were not achieved, instability persists in some areas

### ➤ Stable

#### ○ Coal

- ❖ Indonesian production and exports have steadily increased and it is now among the largest coal exporters



### ➤ Unstable

#### ○ LNG

- ❖ As is well-known, existing Japanese LNG contracts will be reduced to one quarter of their present level after the 2010-2011 contract expiration (from 12 to 2-3 million tons per year)
- ❖ Furthermore, instead of the usual 15-20 year period, the contracts will be renewed for only ten years
- ❖ They did reaffirm that the contracts themselves would be honored

#### ○ Oil

- ❖ PSC terms are subject to fudging around the edges (e.g. cost recovery)

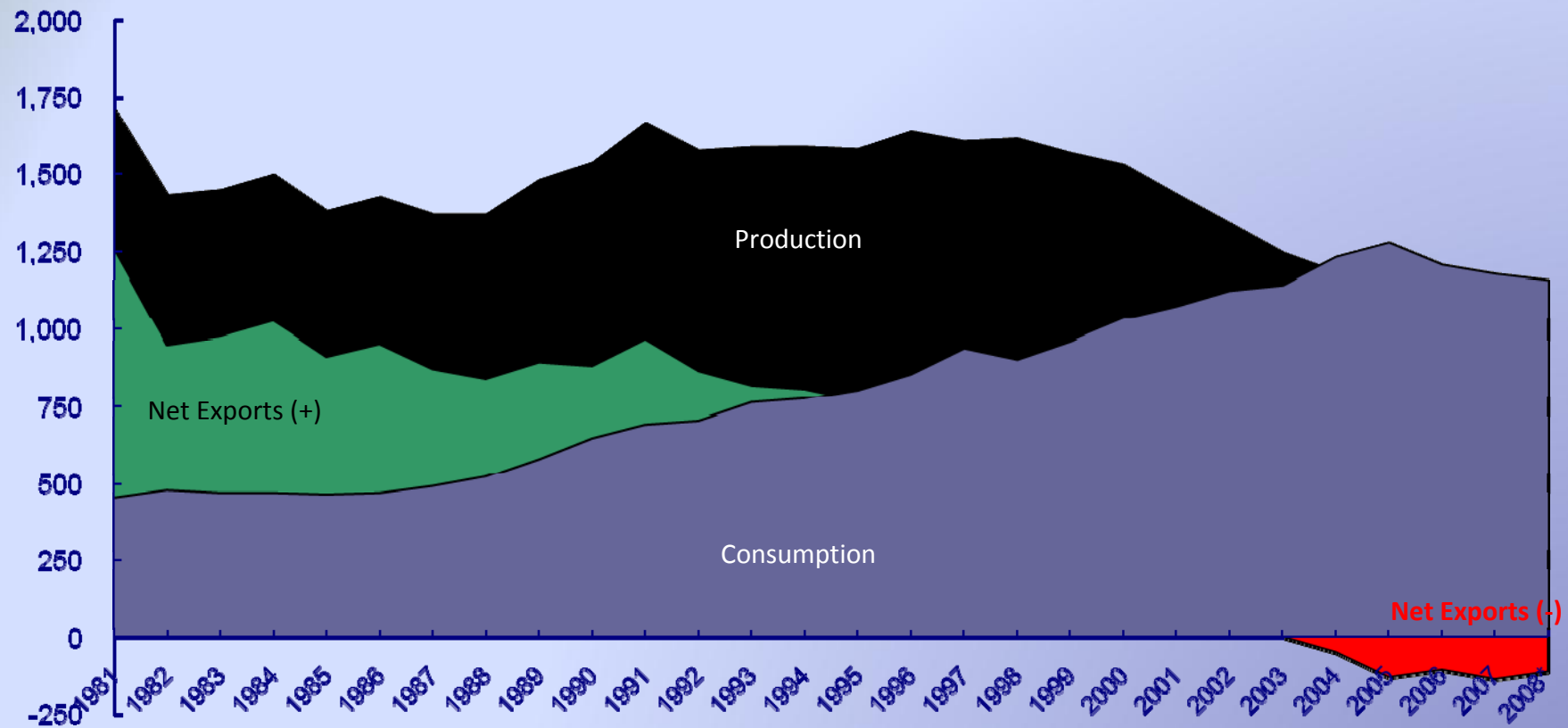
**How might such instability be rectified?**

# Agenda

- Background
  - Diplomatic and Economic Relations
  - Energy Relations
- Japan-Indonesia Economic Partnership Agreement (JIEPA)
  - Background and Purpose
    - ✧ Japan
    - ✧ Indonesia
  - Negotiations
  - Provisions
    - ✧ General
    - ✧ Energy-specific
- Results with Respect to Energy
  - Direct/Short term
  - Indirect/Long term
- Lessons Learned
  - Focus: Energy Supply Guarantee
- Conclusion & Implications
  - The Pitfalls of International Agreements

# Energy supply guarantees were not forthcoming because production was decreasing while consumption was increasing

Oil supply-demand balance and net exports, '000 b/d



# Exploration and production was in decline while new acreage is in remote areas lacking basic infrastructure

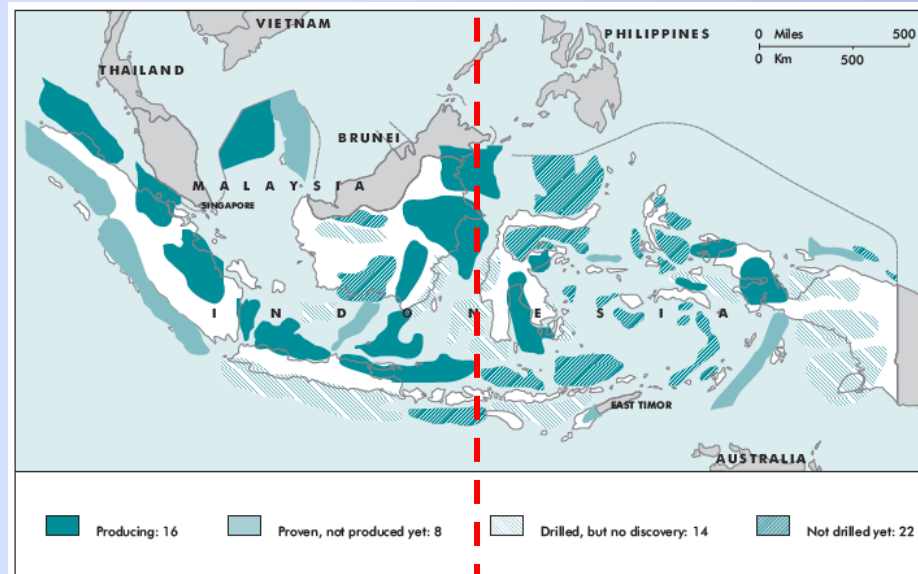
## Exploration Wells

	2000	2001	2002	2003	2004	2005	2006
Offshore	53	49	43	25	28	19	31
Onshore	29	57	45	39	43	49	33
<b>Total</b>	<b>82</b>	<b>106</b>	<b>88</b>	<b>64</b>	<b>71</b>	<b>68</b>	<b>64</b>
<b>Discovery</b>	<b>44</b>	<b>55</b>	<b>46</b>	<b>15</b>	<b>26</b>	<b>30</b>	<b>23</b>
<b>Success ratio</b>	<b>54%</b>	<b>52%</b>	<b>52%</b>	<b>23%</b>	<b>37%</b>	<b>44%</b>	<b>36%</b>

## Reserves

	1990	1995	2000	2001	2002	2003	2004	2005	2006	2007
Proven	5.10	4.98	5.12	5.10	4.72	4.73	4.30	4.19	4.37	3.98
Potential	5.80	4.13	4.49	4.65	5.03	4.40	4.31	4.44	4.56	4.41
<b>Total</b>	<b>10.90</b>	<b>11.00</b>	<b>9.61</b>	<b>9.75</b>	<b>9.75</b>	<b>9.13</b>	<b>8.61</b>	<b>8.63</b>	<b>8.93</b>	<b>8.40</b>

## Sedimentary Basins



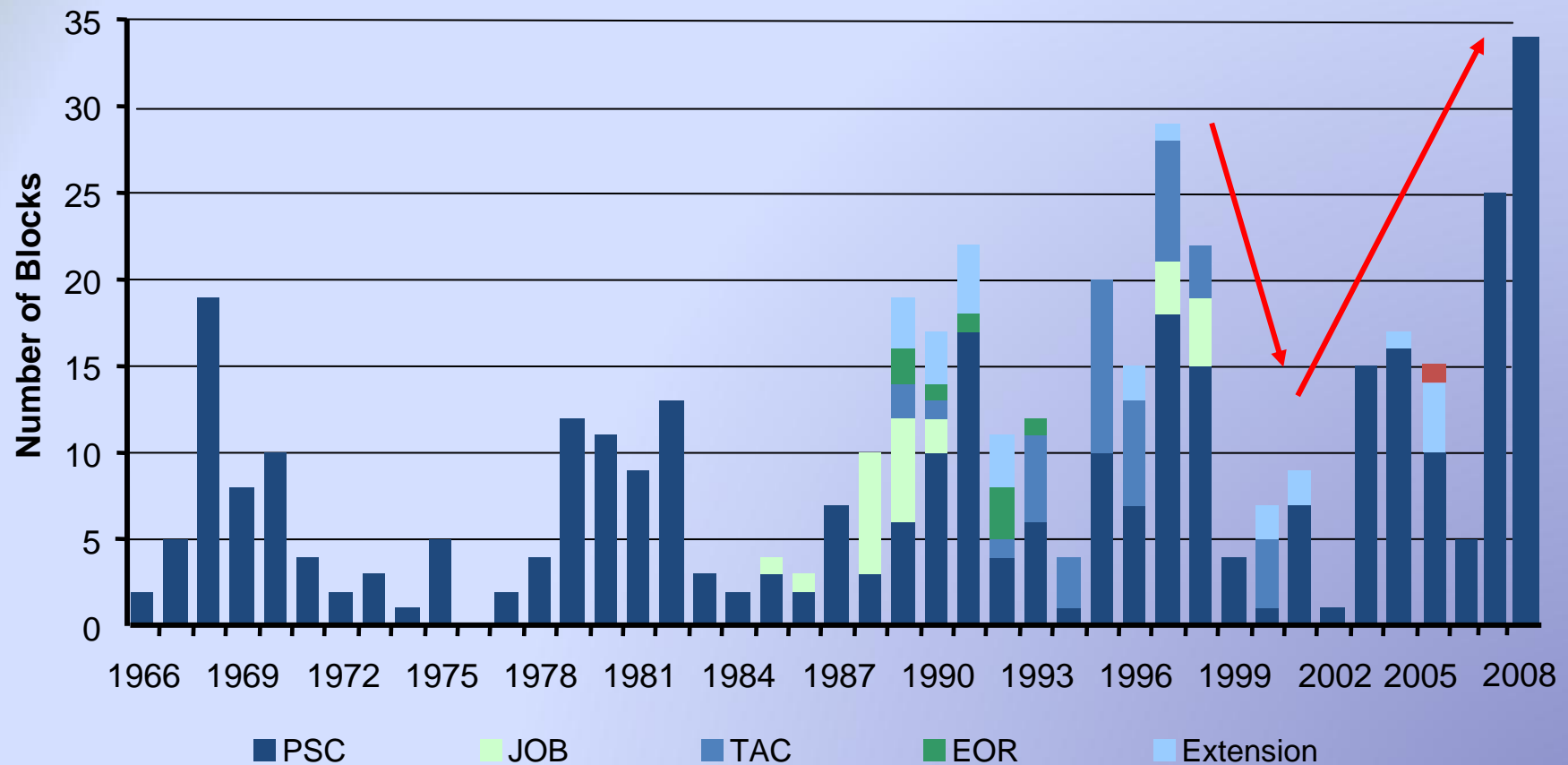
## Lesson Learned#1:

# Facts on the Ground > Hopes & Wishes

- In light of the domestic energy supply/demand balance, supply guarantees were unrealistic
- International agreements cannot single-handedly overcome fundamental market, economic, and political realities

# Upstream licensing activity dropped dramatically after the 1998 Crisis, but is now back up to pre-crisis levels

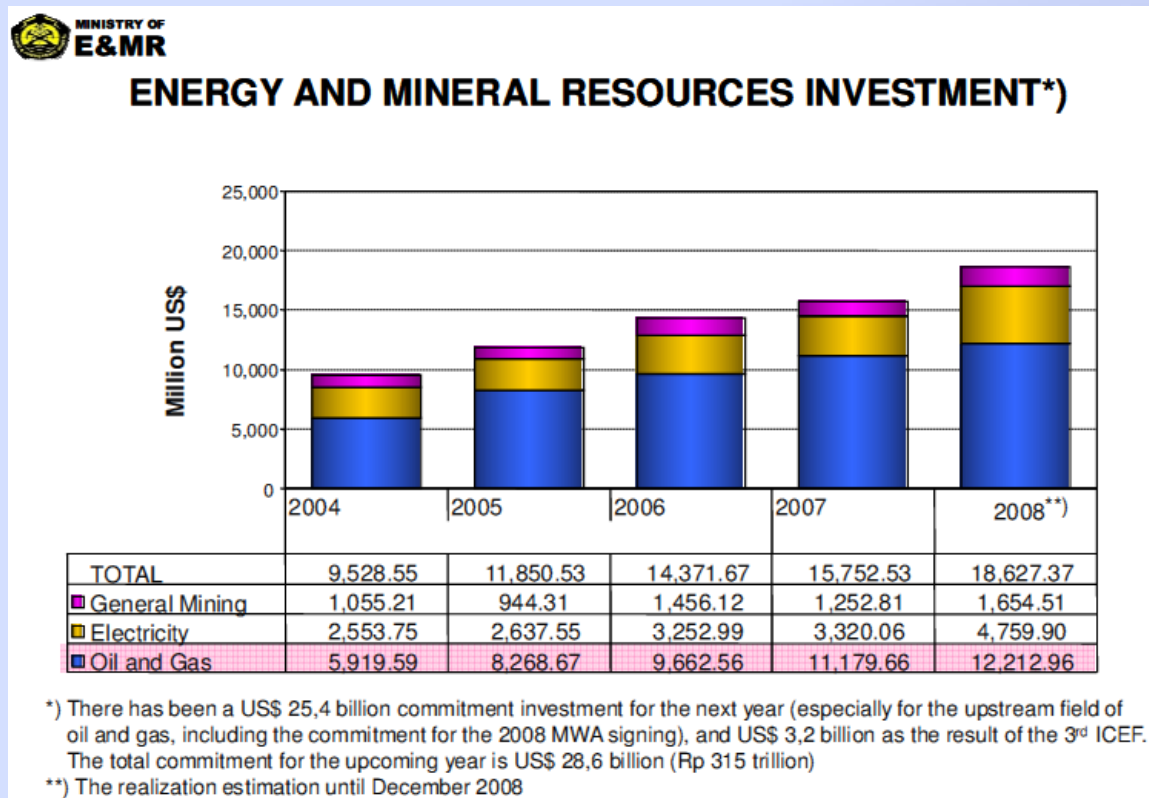
## Tendering and Licensing Activity in Indonesia



Source: Interview Presentation

# As is actual upstream investment increasing, but it has yet to make up for the disastrous post-Suharto decrease

- Upstream investment is projected to reach \$25.4 billion in 2009



**Investment is the key to restoring production and increasing security**

## Lesson Learned#2:

### Investment > Trade

- Given the capital-intensive nature of the energy business, investment is more important than trade in increasing energy supply and security



## Given the impossibility of supply guarantees, increasing investment is a decent second best

Facts on the Ground > Hopes & Wishes

Investment > Trade

The investment-related provisions of JIEPA will be more important to energy supply and security than the directly energy-related provisions

# Agenda

- Background
  - Diplomatic and Economic Relations
  - Energy Relations
- Japan-Indonesia Economic Partnership Agreement (JIEPA)
  - Background and Purpose
    - ✧ Japan
    - ✧ Indonesia
  - Negotiations
  - Provisions
    - ✧ General
    - ✧ Energy-specific
- Results with Respect to Energy
  - Direct/Short term
  - Indirect/Long term
- Lessons Learned
  - Focus: Energy Supply Guarantee
- Conclusion & Implications
  - The Pitfalls of International Agreements

## JIEPA can be judged a success in many fields

The Agreement is wide-ranging, encompassing the entire economic relationship

- Revitalize the bilateral governmental relationship
  - in the face of recent deterioration and the increasing prominence of other actors
- Trade
  - 93% of trade by value will be tariff-free
- Investment
  - Some improved forums for bilateral discussion and deliberation
  - Depending on implementation, major improvements in investment environment and Most Favored Nation-based treatment investors
- Capacity building
  - Manufacturing Industry Development Centers
- Movement of Natural Persons
  - 1,000 Indonesian nurses and caregivers to Japan over two years
- Increased bilateral policy and regulatory dialogue
- Internal policy coordination
  - The process of negotiating a comprehensive EPA forces ministries to talk to each other at levels below where normal coordination takes place
  - New coordinating sub-committees and bodies created

# There is substantial potential for progress in energy relations by means of non-energy JIEPA provisions

## Energy-related JIEPA provisions

### ➤ Investment:


- Foreign investors in Indonesia frequently face differential rates of taxation on similar investments
- If followed through upon effectively and applied consistently down to local levels, these investment principles could provide significant benefits to Party investors

### ➤ Dispute Resolution:

- Mechanism has not yet been used, but may be effective in helping to resolve disputes (say, over investment)

### ➤ Business Environment Enhancement:

- While another forum probably won't hurt, it is unclear what concrete improvements can come about



**Too soon to judge the effectiveness of non-energy provisions**

## There is also substantial potential for progress in pre-existing but parallel energy cooperation efforts

### Separate but parallel cooperation

#### ➤ Energy Efficiency

➤ JICA-MEMR: Workshop on Energy Conservation Improvement and Efficiency (2007-ongoing)

#### ➤ Nuclear

➤ MEXT: Forum for Nuclear Cooperation in Asia (FNCA) [not just Indonesia]

➤ Institutional capacity building [bilateral]

#### ➤ Bio-fuels

➤ JJC-KADIN: Industrial Joint Forum on Investment's Bio-fuel Sub-Working Group – Industrial Strategy Proposal [Policy Recommendations]

#### ➤ Coal

➤ METI-MEMR: Upgraded Brown Coal (UBC) plant in Kalimantan inaugurated Dec.4 2008 (2001-ongoing)

➤ Coal-to-Liquids (CTL) Technological and investment support from Japan to produce 2% of national energy supply by 2025

**While most of these efforts pre-date JIEPA, having the cooperative principles behind them enshrined in an international agreement cannot but help their cause**

# Agenda

- Background
  - Diplomatic and Economic Relations
  - Energy Relations
- Japan-Indonesia Economic Partnership Agreement (JIEPA)
  - Background and Purpose
    - ✧ Japan
    - ✧ Indonesia
  - Negotiations
  - Provisions
    - ✧ General
    - ✧ Energy-specific
- Results with Respect to Energy
  - Direct/Short term
  - Indirect/Long term
- Lessons Learned
  - Focus: Energy Supply Guarantee
- Conclusion & Implications
  - The Pitfalls of International Agreements

# A Cautionary Note: What is agreed in international agreements is not always what it seems

Countries are sovereign and cannot readily be compelled

## Ex-post Reinterpretation of Terms

- Subsequent to JIEPA entering into effect, one party can inform the other that it chooses to interpret the terms of the agreement in a way that conflicts with the other party's understanding
- For example:
  - The parties could disagree on the classification of goods subject to tariff reductions or market access requirements (e.g. steel)
  - One party could unilaterally decide that certain issue areas or government bodies are not subject to the terms of JIEPA
- Why does this matter?
  - What good is an agreement if it can be changed at will ex-post to favor one party's interests over the other's?

## Options for Dispute Resolution

- One option would be to launch an official dispute at the WTO
  - which may or may not be successful and,
  - would certainly negatively impact overall bilateral relations
- Another option would be to resort to other forms of leverage, say:
  - In the case of Japan, reducing access to preferential loans, or
  - In the case of Indonesia, delaying investment approvals in unrelated areas
- The Bottom Line: The broader relationship severely constrains freedom of action in case of disputes



WORLD TRADE ORGANIZATION



JFC JAPAN FINANCE CORPORATION

JBIC JAPAN BANK FOR INTERNATIONAL COOPERATION<sup>47</sup>

## Lesson Learned#3:

# Principles > Rules to be Followed

- Given the difficulties of enforcement, JIEPA lays out principles (e.g. non-discrimination in investment and taxation, cooperation, etc.) diplomats can point to during discussions and negotiations

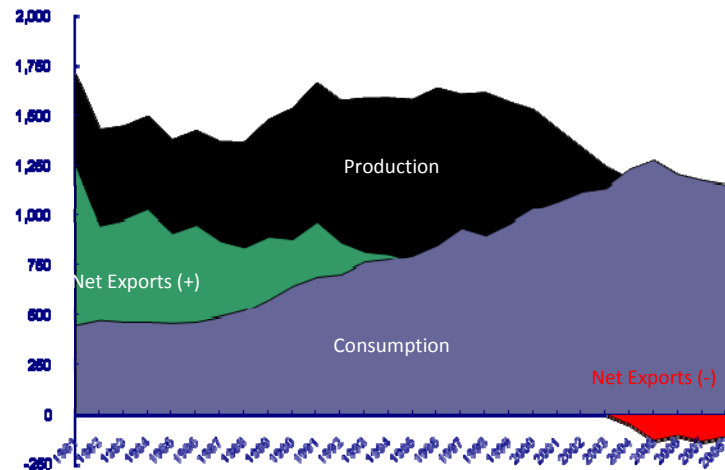


# That said, efficiency improvements coupled with investment & technology cooperation will improve S/D balance

Implementation is vital

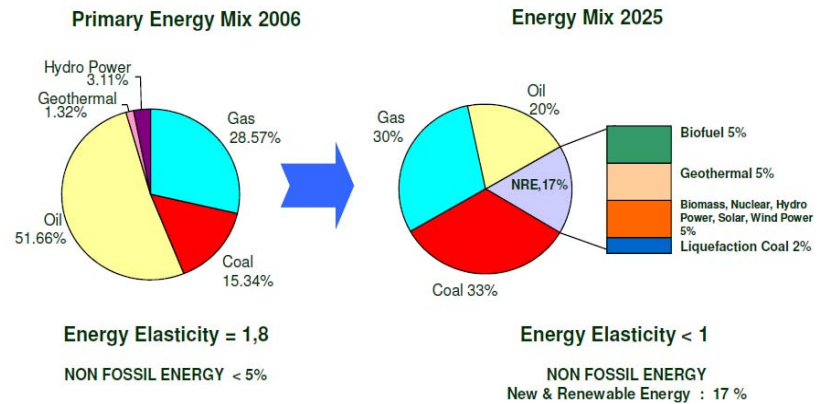
## Efficiency and Investment

Oil supply-demand balance and net exports, '000 b/d



## Technology Cooperation

Target Energy Mix, Presidential Regulation 5 (2006)



## In Conclusion

Facts on the Ground > Hopes & Wishes

Investment > Trade

Principles > Rules to be Followed

Overall, JIEPA is symbolic but important

The effectiveness of JIEPA regarding energy security and supply hinges on implementation of investment and business environment measures that can help to change the unfavorable facts on the ground hindering:

- investment
- the development of Indonesia's natural resources
- energy security for both nations

有難うございます

Terima Kasih Banyak

Thank You

