

Roles of International Standards in Indonesian Small and Medium Enterprises (SMEs) in the Context of CHINA-ASEAN Free Trade Area (CAFTA)

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Abstract: Indonesia is one of the fastest growing developing countries in Southeast Asia and has a bright future, as it is estimated to become the 10th largest economy in the world by 2020. In the year 1995, together with several ASEAN leaders, the then president of Indonesia signed the WTO Agreement in Geneva, Switzerland. By joining the WTO Agreement, Indonesia established common markets (free trade zone) with several other countries in its region and agreed to follow WTO principles. The first common market came into force 2 years later. Indonesia entered into the China – ASEAN Free Trade Area (CAFTA). The result was unsatisfactory. In the year 2012, it is noted that its balance of payments has a minus with the total amount of US\$ 7 Billion in trading activity against China. What is the main problem behind this number? It is found that there are 11 industrial sectors which are most affected by the establishment of CAFTA. The industrial sectors are steel, textiles, jute, horticulture, machinery and equipment, electronics, furniture, toys, foods and beverages, and shoes. Further, it is found that Small and Medium Enterprises (SMEs) in each sector cannot compete with China's products both at the local and global market because of lack of knowledge about standardization. Ultimately, if there is no further solution, these sectors are going to collapse. In order to compete with foreign products in FTA, SMEs in Indonesia have to adopt and establish ISO as a guideline in their business activities so that they are able to exist for supplying both the local market and the global market, especially in the CAFTA region. This can be accomplished by several kinds of strategy and of course with the support of the government of Indonesia. There are several steps suggested, such as identifying the availability of international standards for 11 industrial sectors, accelerating identical adoption of ISO to Indonesian standards (SNI), analysis of industrial competences, analysis of conformity assessment bodies' competences, analysis of national differences, market operation - technical regulation, and educating consumers as the final users.

Keywords: CAFTA; ISO International Standards; Dismantling Trade Barriers; Indonesian SMEs.

1. INTRODUCTION

Changing in Nature of an International Business and the Roles of WTO in Free Trade Area:

At present, there is no country which is able to fulfill its necessity for consuming every good and service itself because of limited resources and competitive advantages. A country which is able to produce some particular product may focus to produce and export it to another country in order to gain a profit from an international trade. Let us say the US and Japan. They focus on producing high technology products such as computer, automobile, electronic stuffs, and software. By exporting to the other countries, especially developing and emerging economies which are mostly in Asia and South America, they may gain several advantages. They may establish their Multinational Companies (MNCs) as the main actor in the international trade for conducting their branches and manufacturers in developing and emerging economies such as:

India; Indonesia; Vietnams; Brazil; South Africa; and etc. By Foreign Investment (FI) policy, they may build and develop their manufacturers in each branch and gain low level of production costs because of low employment wages and low cost of raw materials. Microsoft as one of the biggest MNCs from the US, has so many branches in developing countries as it realizes that an international business provides a high proportion of income for both the MNC itself and the US as the home government for tax of repatriation of the investment yield in several economic regions.

Table 1 World View (Percentage Regional Distribution of IT Sales For Selected Companies in 1993)

PARTICULAR COMPANY	NORTH AMERICA	EUROPE	ASIA
IBM	41	33	16
sFujitsu	6	26	65
HP	51	34	9
NEC	6	4	88
Compaq	45	38	5
Canon	30	29	37
Sun Microsystems	51	24	25
NTT	0	0	200
Microsoft	56	30	9

(Source: *The economic Times, Dec.26.2003*)

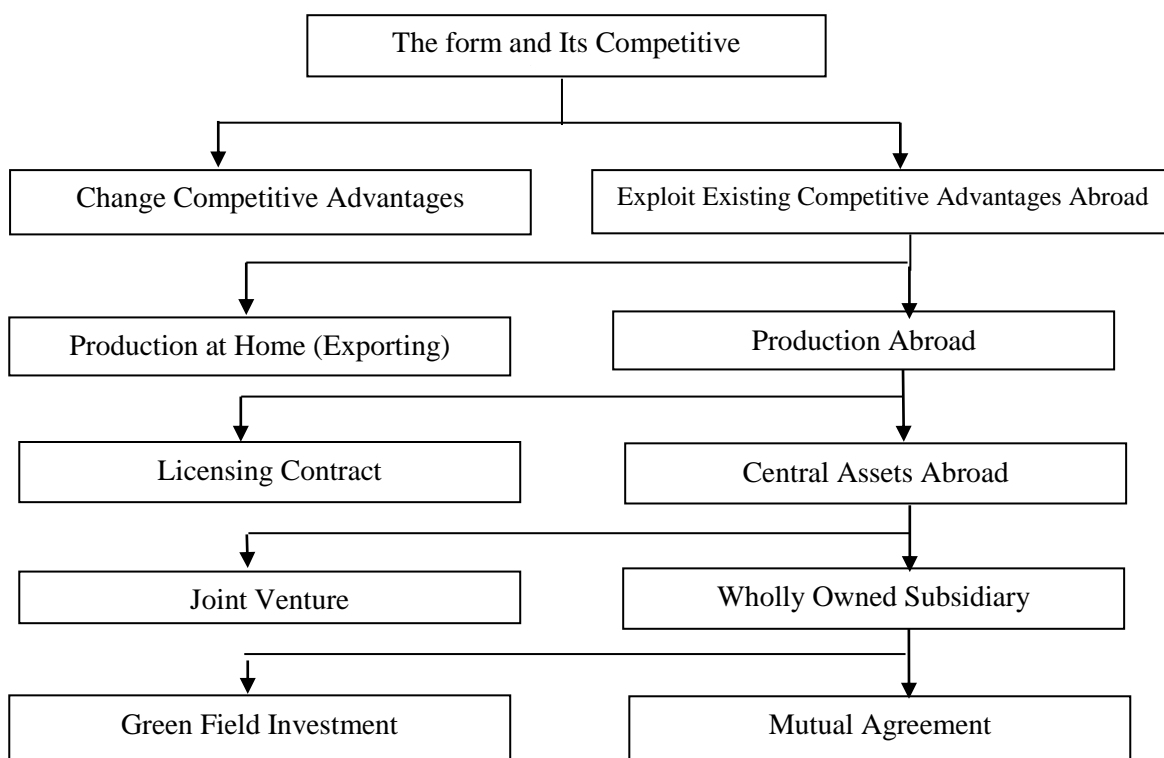
While developed countries like The US and Japan focus on high technology products, on the other hand, developing countries focus on exploring their natural resources, refining, exporting and providing better monetary and fiscal policy, raw materials, labors, and infrastructure for engaging with FI through public - private partnership or private - private partnership.

Let us see Indonesia as one of the most interesting country for the FI destination with its strong economic indicators. After its independence in the year 1945 from the Netherlands, Indonesia has become a major democratic country in Asia and the leader of the Association of Southeast Asia Nations (ASEAN). With a present population of more than 230 million people, GDP per capita of US\$ 3,500 per year , level of unemployment is less than 7% from the population, economic growth in average is around 6.3 - 6.5% (2009 – 2012), foreign loan of less than 26% from its GDP, and reserves for about US\$ 116.4 billion in April 2012, Indonesia is expected to be the 10th largest economy in the world after China, The US, India, Japan, Brazil, Germany, France, Russia and the UK in the year of 2020.

There are so many MNCs from the US, Japan, and the EU Countries which want to invest and conduct an international business in this tiger economy, especially after getting an investment grade (BBB-) from the Fitch in 2011. As a host country, Indonesia at present of course has to face several challenges because of changing in the nature of international business environments. The government is unable to ignore the role of MNCs in its domestic market. By their far reaching impact of high technology, for example Kentucky Fried Chicken (KFC) is able to spread its business in each province in Indonesia and wins the competition against local restaurants. Wall Mart is able to win the competition with traditional market, and Unilever which is able to cover everybody needs for daily products in this country are also gaining the same thing. All about that case is because of MNCs are guided by the International Standards so that their products are able to penetrate to every market in each country and gain huge level of income from global market.

Actually, there are so many modes of international business, such as: licensing; exporting; joint venture; wholly owned subsidiary; and etc. But the thing is MNCs has to spread its business in overseas market on the basis of its competitive advantages.

Table 2 Modes of Foreign Investment



Competitive advantages imply that countries prosper by taking advantage of their assets in order to concentrate on what they can produce better. Bigger markets, domestic as well as overseas, will help these countries produce more and reap economies of scales. Liberal trade policies that allow unrestricted flow of goods and services will result in expanded market.

On the other hand, protection and perpetual government subsidies lead to bloated, inefficient companies supplying consumers with outdated and unattractive products. Ultimately, factories close and jobs are lost despite protection and subsidies. If other governments pursue such policies overseas, markets contract and world economic activity is reduced. Hence the need for free and open trade is emphasized upon.

If we trace back, in the year 1995, the then president of the Republic of Indonesia, Suharto, together with several leaders from ASEAN countries, signed the World Trade Organization (WTO) Agreement in Geneva, Switzerland. WTO which is the embodiment of the Uruguay Round results and the successor to the General Agreement on Tariffs and Trade (GATT) now has a present number of member's stands at 151. As a member of the WTO, Indonesia has to follow and cope with its principles, rules, regulations, mechanisms, and activities. The WTO has nine principles, as follows:

1. Transparency;
2. "Most Favored Nations" or MFN Status;
3. National Treatment: Non-Discrimination within a Country;
4. Free Trade Principle: Optimal Utilization of Resources;
5. Dismantling Trade Barriers;
6. Rule-based Trading System;
7. Treatment of Least Developed Countries;
8. Competition Principle; and
9. Environmental Protection.

Several purposes are also there, especially for the implementation of a common market (free trade zone) For Indonesia, the implications are the establishment of China - ASEAN Free Trade Area (FTA), India – ASEAN FTA, New Zealand –

ASEAN FTA, and Korean FTA, and the ASEAN Economic Community (AEC). The first FTA came into force in 2010. Indonesia has entered into China – ASEAN FTA (CAFTA). After two years, the government Indonesia has realized that the balance of payments was a deficit in its current account with the total amount of US\$ 7 billion against China. Indonesian products could not compete with China’s products in both local and global markets. Small and Medium Enterprises (SMEs) are going to collapse. China could produce in several levels of product quality, from the lowest till the highest quality, following each standard in every country as well as an international standard.

2. NEED FOR ISO AS INTERNATIONAL STANDARDS TO IMPROVE THE QUALITY OF INDONESIAN PRODUCTS IN CAFTA REGION

At the end of 2011, it is found that there are 11 industrial sectors in Indonesia which are most affected by the implementation of CAFTA. They are: steel; textile; jute; horticulture; machineries and equipments; electronics; furniture; toys; foods and beverages; and shoes industrial sectors.

Table 3 Indonesia – China Export and Import in the year 2011 For 11 industrial sectors

No	Particular Industrial Sector	Export Indonesia to China (In US\$)	Import Indonesia from China (In US\$)	Surplus/ Deficit (-) (In US\$)
1	Steel	62,609,562	1,899,043,446	-1,836,433,884
2	Textile	195,345,155	959,163,899	-763,818,744
3	Jute	56,519,318	507,627,736	-451,108,418
4	Aluminum	7,204,237	289,699,066	-282,494,829
5	Horticulture	16,087,203	192,218,463	-176,131,260
6	Equipments and Machineries	1,251,463	173,764,456	-172,512,993
7	Electronic	1,342,152	139,076,003	-137,733,851
8	Furniture	7,657,020	94,250,385	- 86,593,365
9	Toys	6,836,788	89,571,912	-82,735,124
10	Foods & Beverages	4,094,599	68,926,209	- 64,831,610
11	Shoes	64,366,024	89,041,635	- 24,675,611

As we have seen at 11 most affected industrial sectors above, China is very strong and dominant in each industry, and Indonesia has a deficit in trading activity for almost every kind of important daily products such as foods and beverages, toys, electronics, and furniture as well as an intermediary product such as aluminum, steel, jute, and textile. The reason behind that is the China’s products are compatible with every standard. China is able to produce a product in accordance with International Standards (ISO), American Standards (ASTM), Japan Standards, Korean Standards, and of course Indonesian Standards, or known as “Standard National Indonesia (SNI)”. China’s entrepreneurs have done economies of scales for doing a production in a very huge number of quantity because of their low labor wages and big number of skilled labors so that they are able to reduce the price of the product because of the low cost of production and become competitive in the global market. The government of China also provides good infrastructure such as nonstop electricity, low interest rate of borrowing capital, transportation, and policy for devaluing its currency (Chinese Yuan Renminbi/CYN) toward its original value in order to impose Chinese entrepreneurs for doing an international business in order to gain much profit from an arbitrage opportunity in their currency towards foreign currency as well as increasing its national reserves.

While China is ready for entering the CAFTA, from the year 2010 Indonesian entrepreneurs and consumers have had so many problems. All of them is because of the lack of knowledge in standardization area. As per WTO principles, a country which is joining as a member of the WTO has to follow its principles. One of them is establishing a free trade principle by dismantling trade barrier. It means that each member has to reduce the tariff barrier and impose technical barriers to trade, which is standardization. Standardization is a “norm”, and a minimum requirement in safety, health, and quality of production and distribution of goods and services to the consumers. On an international level, we know about International Organization for Standardization (ISO) as an apex body in standardization area and its products such as: ISO 9001: 2008 for Quality Management System (QMS); ISO 1:2002 for Geometrical Product Specifications (GPS); and etc. At present ISO has 164 members which are divided into member body, correspondent member, and subscriber member. Indonesia through “Badan Standardisasi Nasional (BSN)” represents itself as an ISO member body. BSN has several functions, same as ISO but it is on a national level.

As we mention above, because of the lack of knowledge about standardization, Indonesian products cannot compete with Chinese products. In order to compete with China's products in CAFTA region, it is obvious that SMEs at 11 industrial sectors have to adopt ISO as an international standard in order to increase their quality of products. By doing so, hopefully export and import of Indonesia and China will be balanced, and the deficit will be less.

3. THE STEPS FOR IMPLEMENTING ISO AS INTERNATIONAL STANDARDS FOR INDONESIAN SMES AT 11 INDUSTRIAL SECTORS MOST AFFECTED BY CAFTA

SMEs as pillar of Indonesian economy which have contributed around 60% of its GDP and provide a high level of employment are going to collapse at present. In order to cope with international business challenges, the implementation of ISO for Indonesian goods and services is a must. In order to help SMEs for their existence both at local and global markets, especially in CAFTA region, knowledge of the application of ISO as international standards has to be implemented. It is a big homework especially for the government as an agent of change. The roles of the government as an engine for building an infrastructure of standardization, spreading information, educating industries and consumers, and giving an incentive are needed.

In my opinion, there are several strategies as the steps that the government of Indonesia may pursue in order to win the challenges of CAFTA especially for 11 industrial sectors above which is by application of ISO for Indonesian product and services, and how the application works. The steps are as follows:

1. Identifying an Availability of ISO International Standards and Indonesian Standards (SNI) for Each Business Operation at 11 Industrial Sectors Which is conducted by SMEs:

First of all, the government may identify the availability of ISO and SNI documents for each product covered at 11 industrial sectors most affected by CAFTA. Whether every document which is needed is available or not; How many documents have to be revised?; And How the businessman may able to get the documents in term of their distribution?.

While the documents are available, we must know that SMEs are using them for guiding their business. When they do not use international Standards or Indonesian Standards it means that, it is very hard for them to join the global and even local competition as FTA has already existed and the competitors from China are more knowledgeable in standardization area.

2. Establishing an Identical Adoption of ISO International Standards to Indonesian Standards (SNI) for Accelerating the Availability of Standardization Documents Especially for 11 Industrial Sectors:

We all know in order to produce one document of standard for each business, it needs time. The time may vary, it can be several months to a year, or more than one year, depends on the complexities of its parameters. Since CAFTA has come into force from the year 2010 and SNI as a national standard needs to be revised regularly, it is obvious that identical adoption of ISO to SNI is a must in particular goods and services. At 11 industrial sectors above, we can say that parameters in ISO's documents are higher than SNI, and ISO is also accepted in every country. By adopting ISO to SNI in an identical way, it will reduce the time for preparing Indonesian standards, and ultimately the purpose for maintaining the availability of standards in each sector is reached because of the reason of the language as well.

3. Analyzing and Introducing National Differences Products in order to Promote Indonesian Original Products in International Markets:

Based on article 2.2 of the WTO Agreement, technical rules are conducted in order to accelerate an international trade between countries. It has to be suited with the national defense safety, lawful practices, health and safety for animals, plants and their environment. Further, based on the F Annex 3 Code of Good Practice for Preparation, Adoption and Application of Standard from Technical Barrier to trade - WTO, Indonesia is allowed to submit national differences clause. For example, based on its geographical area or basis of technology, development of SNI is not merely identical with ISO. Indonesia may develop SNI by submitting national differences clause as long it is supported by empirical data and provable.

On the other hand, Indonesia may also promote its original product in order to be adopted as an International standard. For example in the year 2012, BSN has struggled to submit "Tempeh" as Indonesian originally produced in order to be an international product by lodging its parameters in ISO document. "Tempeh" which can be defined as a traditional soybean product originally from Indonesia and made by a natural culturing and controlled fermentation process that binds soybeans into a cake form, now a day is eaten by most people in Indonesia. On average, the national consumption is

about 2.4 million tonnages per year. Also, it has a huge potential to be consumed by every vegetarian in this world, we can mention that India has very huge vegetarian population in this world. Because of its unique and original, Indonesia is able to lodge its parameters as an ISO document. At present BSN is trying to promote it by struggling in regional areas via project document. In the future, we hope that standardization of “Tempeh” will exist and accepted as an international standard.

Further, it is possible for Indonesia in order to identify the others potential national differences product to be promoted in a global market through international standardization.

4. Analyzing the SMEs Competences for Implementing ISO and Giving an Incentive Program:

The most important factors to implement the standardization are competencies and willingness of SMEs as the main actor in producing and distributing goods and services. The implementation of standardization has to consider about the industrial capability to fulfill the eligibilities of international standard whether they are eligible or not.

Standards have to meet with the competencies of each industry, not merely as documentations. If any particular industry is not able to implement what are directing in it, standardization will be useless as it is beyond the competencies of the industry itself.

Based on a survey conducted for 11 industrial sectors above and each SME in them, it is found that there are so many weaknesses in application of standardization in Indonesia. As follows:

- a) Do not know/not yet know about ISO.
- b) Parameters and contents are difficult to implement in a particular industry.
- c) SMEs find a difficulty in getting ISO certification and they think that it increases their cost of production.
- d) SMEs use their own standard based on its experience in the market and demand of the consumers.

In this step, we need to do mapping for getting information about industrial competencies in implementing ISO. The result of mapping will be the basis for giving an industrial incentive program for the purpose of implementing ISO.

The focus of the incentive is for SMEs. Then, the government may give an incentive through its ministry or its relevant chamber of commerce in Indonesia.

5. Analyzing the Capability of Conformity Assessment Bodies (CABs):

The standard will not be able to implement if there is no software for proving the suitability of it in the business operation. From the basis of its evidence, there will be a result known as “statement of suitability in implementation”. However, this statement has to be given by competence institutions.

In implementing ISO for 11 industrial sectors, support from Accredited Conformity Assessment Bodies (CABs) as a competent institution is obvious. Industrial sectors need the availability of CABs which are recognized by international markets in order to examine the parameters of international standards.

In order to maintain the availability and impose the competency of CABs, the government of Indonesia has to do several things:

- a) Identifies the availability of competent laboratories for examining the standards.
- b) Identifies scope of competency and capacity of each laboratory in order to do conformity assessment especially for 11 industry sectors.
- c) Gives an incentive by providing regular training for the laboratory personnel in order to increase their competency.

6. Market Operation through Technical Regulations for Protecting Industrial and Consumer’s Interests:

In order to protect industrial and consumers' interests, the government is suggested to implement technical regulations as per WTO mechanism and national differences. There are so many things which have to be considered to formulate technical regulations:

- a) Facilitating an arrangement of technical regulations based on Good Regulatory Practices (GRP) and notifying its regulations to the WTO.

b) Improving system and doing market operation intensively especially for substandard products that come from China.

To facilitate the market operation, the government needs a systematic procedure which is efficient and effective for both at penetration product phase and at the market phase. The main considerations for formulating its systematic procedures are based on: risk level of health; safety; and environmental impact. The higher the level of risk, it has to be stronger the level of market operation. Airports and harbors are the main point of market operation as they have a responsibility for gathering information for each product comes from abroad in order to do custom duty.

By doing market operation through technical regulations, hopefully substandard products are banned as it has a high level of risk to health and safety for the consumer and the environment.

7. Educates the Consumers as a Final User:

Ultimately, consumers as the final user of products and services have to be educated. There are several steps which can be implemented by the government, such as:

- a) Disseminates the importance of standardized product to the consumers.
- b) Improves awareness of the consumers for choosing a good quality product for the purpose of health, safety, and environmental protection.
- c) Supports Indonesian consumers in using their own product in order to increase surplus in the balance of payments and support the existence of national SMEs in CAFTA regions through persuasive invitation from the government.

4. CONCLUSION

In a global market, there are several modes of foreign investment. Mostly they are divided into two parts based on competitive advantages in every country and its needs such as Change competitive advantages and exploit its existing competitive advantages abroad. By the establishment of the WTO in the year 1995, international business environments as a part of globalization have been changed. Each member has to follow the WTO agreement, including its objectives, principles, mechanism, and procedures. The most obvious objective behind the WTO establishment is in order to impose free trade area in each membership region. Indonesia as one of the fastest growing developing country in Southeast Asia region has joined the WTO agreement from the earlier year. The first implementation of this agreement is CAFTA, in the year 2010. It is found that Indonesian economy was not ready for joining CAFTA. There have been 11 most industrial effected by the establishment of CAFTA from the year 2010, and even SMEs as the main pillar of Indonesian economy is injured on it. Further, deficit in balance of payments was raised. At present year, deficit of balance of payments in trading activity with China is US\$ 7 billion. The reason is that, China's products are in standard quality and low in price because of its knowledge of dismantling trade barriers and economies of scales.

In order to compete with foreign products in CAFTA especially China's products, SMEs at 11 industrial sectors have to adopt and establish ISO as a guide in their business operations. There are several steps which may the government of Indonesia pursue to implement it. The steps are : identifying the availability of international standards for 11 industrial sectors, accelerating identical adoption of ISO to Indonesian standard (SNI), analyzing of industrial competences, analyzing of conformity assessment bodies' competences, analyzing and introducing of national differences, market operation through technical regulations, and at last, educates the consumers. With the implementation of ISO as International Standards, we hope that Indonesian SMEs will be in existence at local and global markets, and ultimately the government can maintain current accounts on the national balance of payments in the future.

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