KEMENTERIAN PERDAGANGAN
REPUBLIK INDONESIA
MINISTRY OF TRADE

Webinar

Review: Paper on Non-Equity Modes (NEMs) Of Trade in Indonesia

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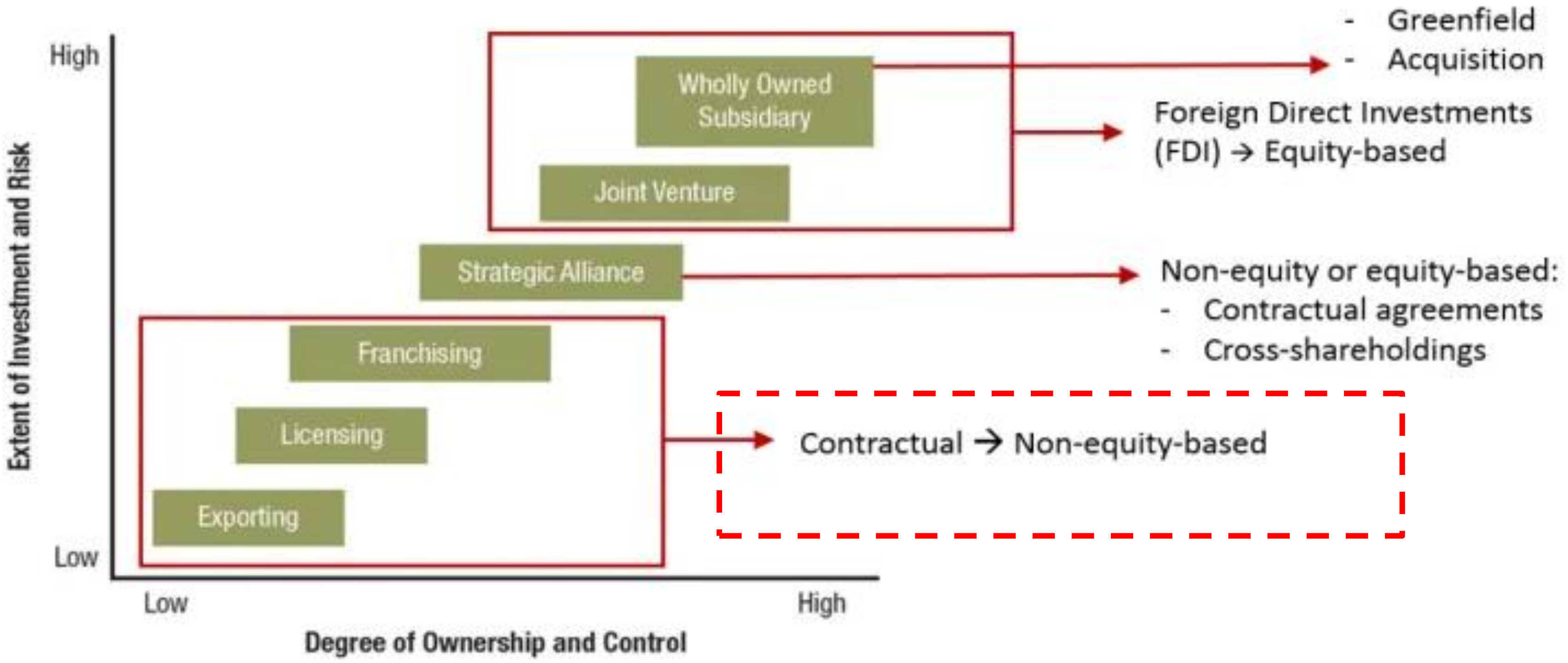
About the Paper

- The paper provides sufficient information about the Non-Equity Modes (NEM) from the Economist perspective.
- The earlier part of the paper describes the characteristics of NEM in Indonesia that covers the scale, scope and several study cases in some industries such as Natural Rubber, Footwear, Hotel, and Convenience Store.
- Some opportunities and challenges of NEM in Indonesia context are also covered in the paper specifically for major industries Natural Rubber, Footwear, Hotel, and Convenience Store.
- The paper adequately explains (5) Five mechanisms on How Indonesia can utilize NEM to promote economic growth through : (1) local firms capability enhancement, (2) investment regulation improvement, (3) improvement of human resources skills and expertise, (4) coordination and connectivity improvement, and (5) global market integration

My takeaways from the Paper

- Implementing and strengthening the regulatory framework for NEM firms could improve export, expand employment and upgrade technologically.
- NEMs are popular among service firms for organizing overseas ventures/operations. In Indonesia, NEMs are commonly adopted by MNCs in specific industries such as labor-intensive industry, hotels, restaurants.
- Yet, NEM is MNC operation mode in overseas market that has limitation on technology transfer from MNCs to host economy compared to FDI.
- NEM is usually chosen by MNCs in the earlier phase of investment to mitigate risks due to *liabilities of foreignness*.

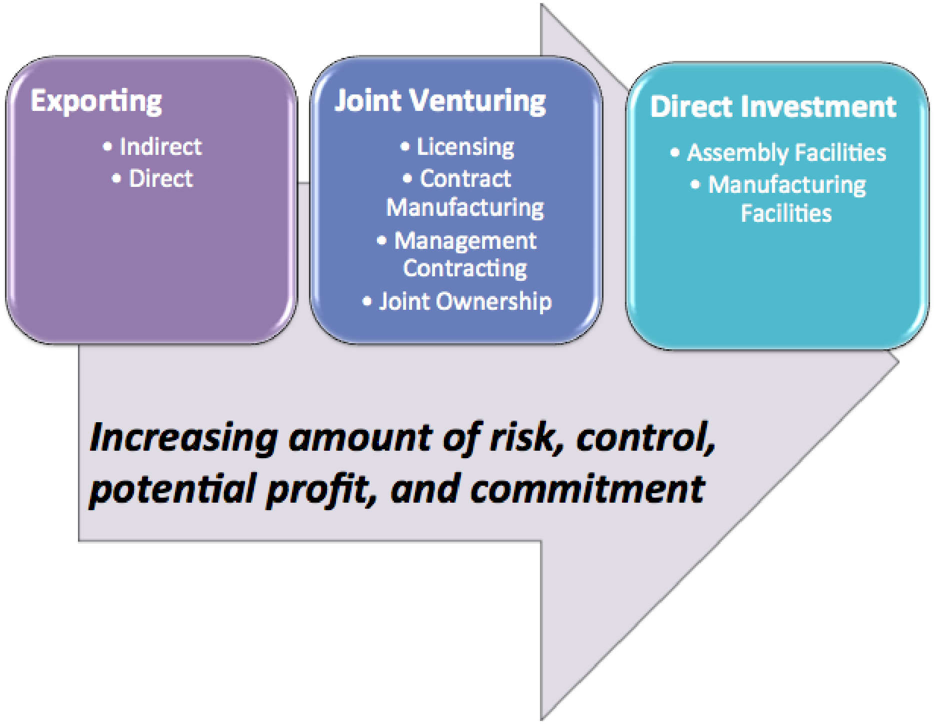
Should Indonesia Promote More NEMs instead of Equity Modes (EMs) ?



Source: Root (1994) Entry strategies for international markets

- Non-equity modes are essentially contractual modes, such as **leasing, licensing, franchising, and management-service contracts** (Dunning, 1988).
- A lower degree of ownership means lower commitment on the investment. The low commitment on the investment reflects firm strategic choice to mitigate business risk in host country. The higher the business risks faced by foreign investor the lower the level of commitment an investor has.
- In general, host country governments prefer EMs to NEMs, because EMs give higher level of commitment and bigger impact of the foreign presence to the performance of local economy.

What we already knew: Business Operation Modes

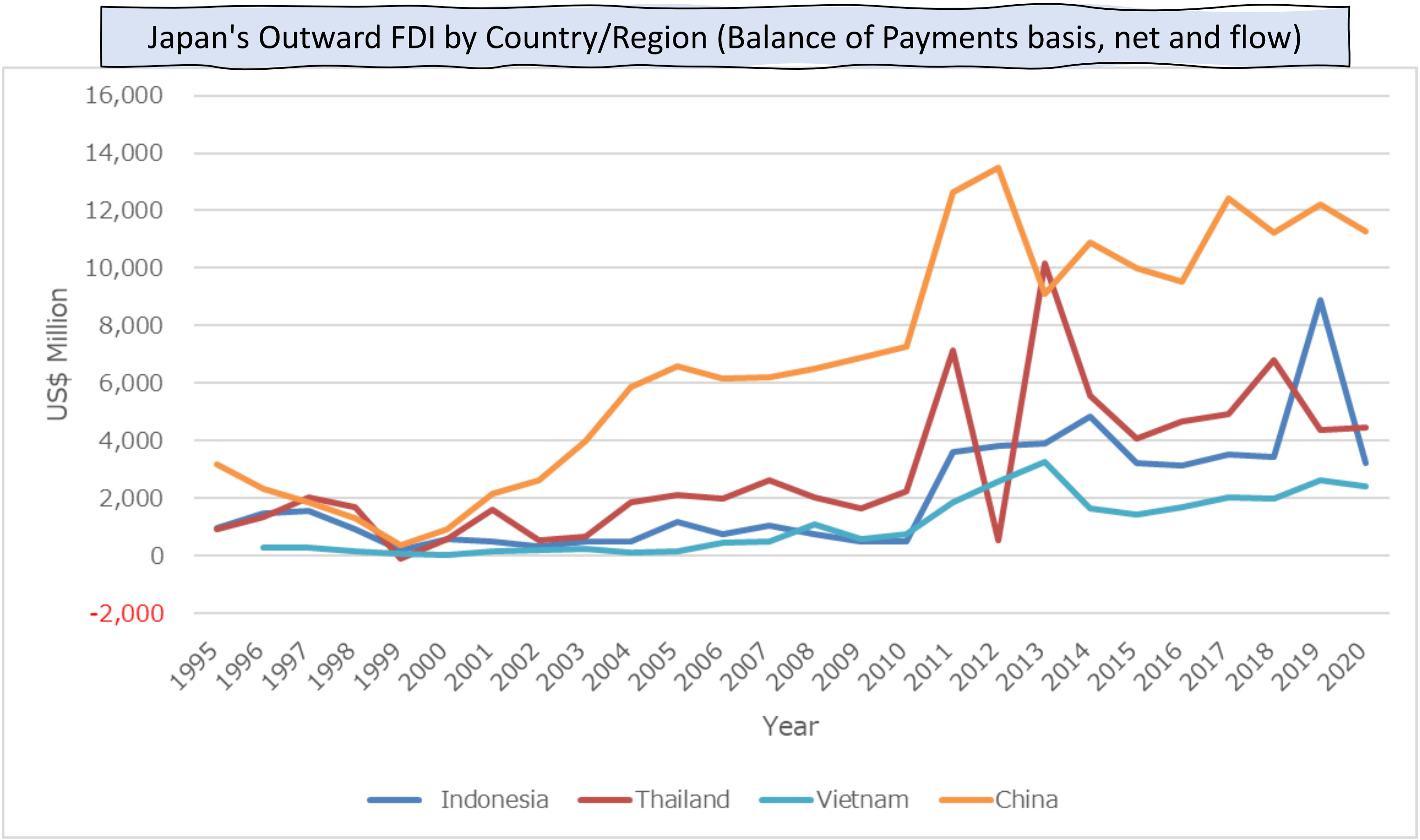


- **Exporting modes:** Foreign Investors start with lesser commitment such as exporting products to explore new markets
- **Joint venturing:** and as the investors adapt to the foreign business environment, they try to find local partners and set up joint venture to overcame the liabilities of foreignness.
- **Direct investment:** as foreign firms operate in the host market, they slowly built their own local knowledge, and decide to invest in the Direct investment mode.
- As the modes move from Exporting to Direct investment, Foreign firms increases the resource commitment and risks at the same time. Therefore, we should be expecting higher contribution from Direct Investment (Equity Modes) than (Non-Equity Modes) in Indonesia economy. Where are we know?→

After 60 years of Indonesia-Japan bilateral relation, we are still talking about Non-market Equity Modes (NEM). Has our relationship lost its spark ?

In 2018 we commemorate the 60th anniversary of Indonesia-Japan relations. For the past 60 years, Japan has been an important and the most vital external source of development for Indonesia. But Japan’s outward FDI to Indonesia relatively low, trend 2.04% per year (2011-2020).

- The growth of Japan’s outward FDI to ASEAN is relatively slow.
- In contrast, Japan’s FDI in China has been growing dramatically in last decade.



Source: JETRO (2021)

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3 Questions that Need to be Addressed by the Author

1. Non-Equity Modes Vs Equity Modes

- In the context of Indonesia economy is recovering from Covid-19 pandemic, do we prefer Non-Equity modes to Equity modes in order to accelerate the growth ?
- Do foreign investors using NEMs only exploit the host country market size for the sake of company's short-term benefit or NEMs also could accommodate host country long term growth?

2. Shifting time from NEMs to EMs

- What do we know about the cross-country variation in shifting time from NEMs to EMs? What is the speed of Indonesia shifting time from NEMs to Ems?
- What are the major determinants that influence the shifting time.

3. Japanese Investors Perspective toward Indonesia economic outlook

- After more than 60 years of economic partnership with Indonesia, what are the major problems faced by the Japanese investors that hinder the investor to shift from NEMs to EMs?

Thank You