

CHAPTER I

INTRODUCTION

A. Background

Palm oil is a commodity found in various countries. This plant is a primary material that widely used for a variety of foods, cosmetics, hygiene products, and can also be used as a source of biofuels or biodiesel. Globally, its usage is increasing massively. Palm oil also appears frequently in the news: its opponents point to good research evidence that careless palm oil development destroys forests, drains peat swamps, destroys rare species, pollutes air and water, triggers climate change, seizes indigenous peoples' property and afflicting the rural poor. The World Bank is in disrepair with the development of the palm oil sector between 2009 and 2011 The World Bank has suspended all funding of palm oil projects worldwide while reviewing World Bank experiences and thinking about how the World Bank should re-engage in the sector to guarantee good results (Colchester, et al., 2011).

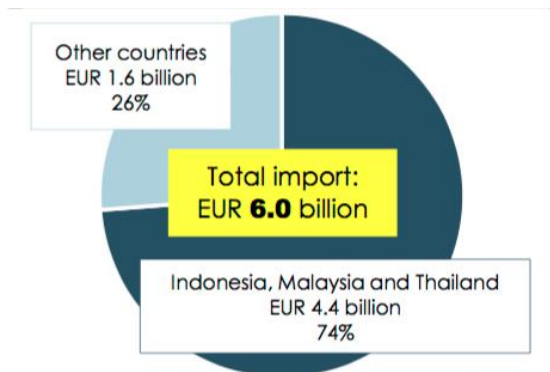
Recognition of these problems also comes from the industry itself, which is driven by consumer concerns, has acknowledged that the method of production must change and that has established the Roundtable on Sustainable Palm Oil (RSPO) through which companies operate through acceptable and valued methods feasibility and certification support. The RSPO aims to distance palm oil plantation from primary forest and areas with high conservation value and prohibit land grabbing, and insist that all land can only be obtained by respecting the rights of local communities and indigenous peoples, including

respecting their right to give or not to give approval for the purchase or lease of land.

To date, most of the attention has been focused mainly on significant palm oil exporting countries, namely Indonesia and Malaysia, which have entered more than 80% of the global market. At present Indonesia is the largest producer and exporter of palm oil. Besides that, the other major exporting country is Thailand and follows several parts of America and Africa. At present, more or less palm oil accounts for one-third of the total 130 million tons per year of vegetable fat that is traded globally per year. The main markets for the growth of the palm oil industry are Europe, India, Pakistan, and China for various needs including Biofuel production (World Growth Report).

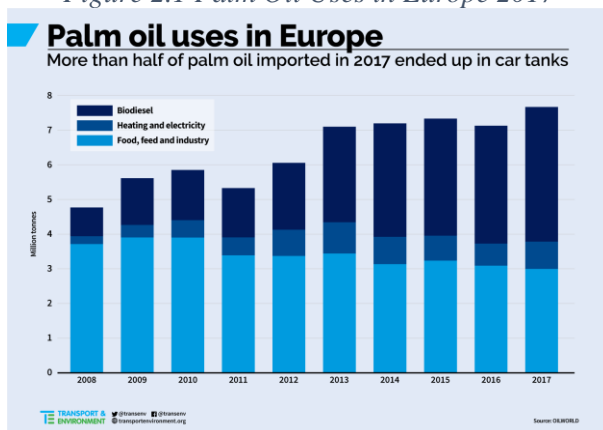
In the EU Renewable Energy Directive (RED), since 2015, mainly for Indonesia, Malaysia, and Thailand as the three largest exporters to the EU, faced considerable pressure. Three countries namely Indonesia, Malaysia and Thailand became the countries that controlled the export of Crude Palm Oil (CPO) by 74% to the EU, which was dominated by Indonesia. Environmental issues and standardization are significant pressures for Indonesia as the world's largest palm oil producer. At present, the European Union occupies the second position as Indonesia's biggest export destination after India, which certainly has an effect on export value with the EU regulation which stipulates the contribution of CPO to biofuels to 0% (Pablo, 2018). The impact its show through the percentage diagram of total EU CPO imports and types of users.

Figure 1.1 EU Good Import (Palm Oil) from Indonesia, Malaysia, and Thailand 2017



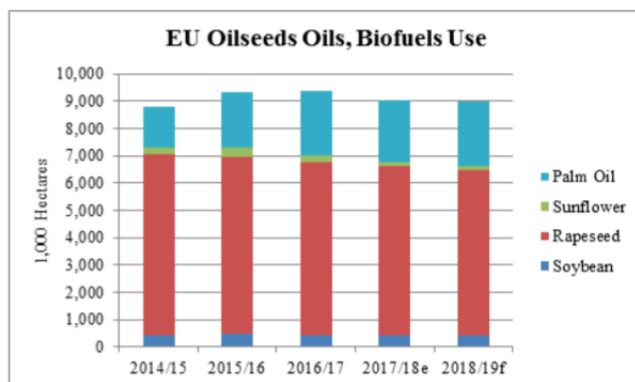
Source: (Copenhagen Economics, 2018)

Figure 2.1 Palm Oil Uses in Europe 2017



Source: (Transport & Environment, 2018)

Figure 3.1 EU Oilseeds Oils, Biofuels Use 2014-2018



Source: FAS Posts

Source: (EU 28 Oilseeds Report Annual, 2018)

From the three figure above, it can describe the magnitude of the influence of the CPO exports of the three countries to meet EU palm oil needs. Where from year to year, exports and imports of palm oil continued to increase, especially in terms of the need for biodiesel/biofuel, each of which continued to increase at the same time becoming the most significant percentage for meeting the use of biofuel production. Moreover, if the determination of the decision to eliminate the contribution of CPO to EU biofuels will undoubtedly be a severe threat to the three countries, especially Indonesia, which currently places the EU as one of its biggest export destination countries.

Palm oil is currently a list of Indonesia's top export products. Based on data from the Central Bureau of Statistics (BPS), palm oil is the most favored export commodity from Indonesia. Its export value of USD 17.17 billion, 28% of Indonesia's total exports in 2017. Inevitably, the prospect of the palm oil industry is now increasingly bright, both in the domestic market and in the world market. This sector will be increasingly

strategic because it has a great chance to play a role as a motorbike for national economic growth and absorb local labor. In the world market, in the last ten years, the use or consumption of palm oil has grown at an average of 8% -9% per year. This growth rate is expected to continue to survive, even if it is closed, possibly increasing in line with the trend of using alternative oils based on vegetable oil or biofuel. The growth of palm oil export means that the diversification potential of the export destination of the palm oil industry in the export market is high enough to improve export performance.

With 36.5 million tons produced in 2017, Indonesia is the largest palm oil producer in the world. However, for environmentalists, the sharp rise of the 8.3 million tons produced in 2001, has sacrificed damaged rainforests and peatlands throughout large areas of Sumatra and Kalimantan in Indonesia as the main reason for Parliament in the EU to ban imports CPO from Indonesia. Where the EU considers the Soybean Industry and other domestic Agriculture, they claim a far more effective and efficient environment that is more friendly to the environment.

Both governments repeatedly deny allegations that refer to Indonesian and Malaysia palm oil as being environmentally unfriendly. In this case, both Indonesia and Malaysia applies various cooperation, certifications related to Crude Palm Oil (CPO), like issuing the Indonesian Sustainable Palm Oil Certification System (ISPO) which aims to increase the competitiveness of Indonesian palm oil in the global market, reduce greenhouse gas emissions, and meet market demands criteria for palm oil that are environmentally friendly.

Regarding the biofuel industry, the EU plans to reduce CPO usage since November 30, 2016. On that

date, the European Commission submitted a reduction in CPO through legislative proposals in the European Parliament. One of the proposed changes is "the proportion of plant-based biofuels that can count towards the EU's renewable energy target will be reduced gradually to 3.8% until 2030". In the next stage, namely first/ single reading, the EU Parliament agreed to adopt the proposal on March 1, 2017. Then a discussion was held again and quite tough on the Council, on December 6, 2017. At the discussion, the European Committee of Industry and Energy issued the European Parliament recommendations that are increasingly burdensome to the CPO Industry: Contributions from biofuels produced from CPO will be reduced by 0% starting in 2021. Then, after a plenary meeting is held, finally, on January 17, 2018, the voting takes place in the EU Parliament. As a result, the proposal that regulates the ban on the use of CPO as a biofuel maker approved by 492 people. Meanwhile, parliament members who rejected 88 people and 107 others said they abstained.

Based on these results, the EU Parliament decided to adopt legislative amendments regarding the revised RED, which means the European Parliament agreed that starting in 2021 the contribution of biofuels produced from palm oil to zero (0%) and calculation of gross energy consumption from renewable energy sources in countries EU member (Hanung, Jalan Panjang Eropa Larang CPO RI, 2018). Furthermore, on June 14, 2018, a trilogue meeting between Parliament, the Council, and the European Commission to discuss RED II related to palm oil from Indonesia and Malaysia which triggered the country to protest vigorously. Now the three parties agreed to provide additional time for Indonesia and Malaysia. The palm oil content in biofuels will no longer be included in the EU climate target and will only be banned entirely by 2030. The EU

has also decided to maintain the volume of imports and will reduce imports of palm oil per year starting in 2023 (European Union, 2018).

B. Research Question

Based on the explanation in the background above, the research question presented by the author is as follows: **"Why did the European Union decide to stop the import of Crude Palm Oil for the use of biofuels?"**

C. Theoretical Framework

Protectionism is a view in a trade that has been present far since hundreds of years before century as illustrated in the philosophy of Plato and Aristotle. According to Aristotle, the best condition for a country is self-sufficiency; various forms of exchanging domestic products with outside money will only have a detrimental effect on the country. Protectionism means deliberate policy by the government as an effort to control imports or exports by providing trade barriers such as quota tariffs that aim to protect industries and producers in the country from competition from outside parties (Kartika, 2013). Protectionism that limits trade competition with outsiders has existed since centuries ago. Even, until recent times, it is still one of the foundations in the choice of trade policies adopted by particular countries in the world.

Amid world trade which is currently developing towards liberalization, protectionism still appears as a trade policy choice. The agenda of world trade liberalization, which began massively since the end of World War II through the GATT instrument, was

considered to have succeeded in significantly reducing the form of trade protectionism in the form of tariffs and believed to be a factor that brought back world trade in its golden age (Hanif, 2014). However, the significant reduction in the application of trade protectionist policy instruments in the form of these tariffs did not last long. The trend of the application of protectionist trade policies rose again in the decade of the 1970s (Hanif, 2014). Almost all countries, including developed countries which are promoters of free trade, apply various forms of new protectionist instruments in the form of non-tariff trade barriers.

The liberalization efforts to create free, multilateral and non-discriminatory world trade are constraining by the development of various instruments of protectionist policy. The conflict between free trade and protectionism policy is a complex problem (Rothbard, 1986); free trade encourages the creation of an open market without government interference which causes the domestic market to be controlled by imported goods. On the other hand, the state is obliged to protect and balance the import and export figures so that the economy in the country continues. Thus, the state is faced with a dilemma in which decisions go in the direction of free trade or choose protectionist policies as a stronghold of the country's economy. In a situation like this, protectionist policies are considered to interfere with the free trade system. Nevertheless, the world trade environment that is truly free and free from government interference has not yet realized. So far no country in the world has been able to liberate trade from various forms of protectionism (McGee, 1996).

Protectionism with the application of policies that hinder trade has emerged since centuries ago. The conventional form of protectionism is old protectionism in the form of import tariffs and quotas, but post-World

War II along with the trade liberalization agenda that focuses on eliminating trade barriers in the form of tariffs, the discourse on protectionism develops from these simple obstacles. In the 1970s new protectionism emerged in the form of the application of non-tariff trade barriers (Hanif, 2014).

Although the purpose of implementing conventional and modern protectionist policies is to side with the domestic producers for their competition with outsiders, the policy instruments used today are far different from before. The conventional form of old protectionism in the form of tariffs cannot be eliminated, but the form of non-tariff barriers from new protectionism continues to grow following the development of world trade. A more functional definition is needed by classifying these forms of modern protectionism in order to make it easier to see the existence and development of understanding and policies (McGee, 1996).

Philip I Levy in *Imaginative Obstruction: Modern Protectionism in the Global Economy* places intent as an essential key that needs to identify in defining protectionist policies adopted by the state (Levy, 2009). It is true that the general intention of the protectionist policy is to favor domestic producers in competition with outsiders, but modern developments require a more functional definition to see specific intentions or intentions from the state in issuing a policy. In the context of world trade liberalization, the definition of functional protectionism is needed to identify the conditions of the readiness of countries in the world in liberalizing trade. Levy classifies protectionism as seen from the nature of its transparent or implicit policies and the form of policy instruments used (Levy, 2009). The three theories in defining protectionism formulated by Levy are as follows.

First, **intentional protectionism**, this form of protectionism is the most transparent form with policy formulations that explicitly favor the domestic industry rather than imports. The policy instrument used is a commonly known instrument in the form of the application of import tariffs, export subsidies, and quotas. Although it has experienced a very drastic reduction since the strengthening of trade liberalization at the global level, this type of protectionism is still very commonly applied in developing countries for manufacturing commodities and almost all countries for agricultural products.

The emphasis in intentional protectionism classification is about explicit goals and transparent instruments. The application of education subsidies and technology development which considered not a type of protectionism will be classified into intentional protectionism when subsidies aimed at developing an industry specifically as implemented by the Japanese government through the Ministry of International Trade and Industry in subsidizing research for semiconductor products for sale dumping into advanced industrial countries.

In addition to the above forms, lately, there have also been other forms that have not invited widespread public reaction but have the same impact on the alignment of local producers, namely the campaign for the use of domestic products. This kind of campaign uses the legitimacy of cultural preservation but is the same aim, namely explicitly giving partiality to domestic producers with transparent instruments. Examples of this type of protection are the "Buy American" campaign, "Cintai Produk-Produk Indonesia," and other forms.

Second, **incidental protectionism** is a form of protectionism that has the same effect as intentional protectionism but works indirectly. In policy terms, this form of protectionism does not appear to explicitly discriminate against foreign products on products originating from domestic producers. It implements the provisions that have strong legitimacy as a requirement for external products that will enter the domestic market. This type of protectionism works indirectly by including non-trade elements such as health, environment, religion, labor protection, et cetera, into the import requirements of products (Rothbard, 1986). The most controversial issue is the application of health and safety standards. These issues represent how issues that were previously considered to have nothing to do with international trade eventually became a reasonable part of the current trade.

Deficiencies found in external products are no longer seen as a defect that can be tolerated but used as a way to eliminate the product as a whole from the domestic market. The most common case is the ban on the entry of European beef products containing bovine spongiform encephalopathy or mad cow disease to the United States (Hanif, 2014). Europeans also applied the same policy to US rice products developed with a genetic engineering system (Genetically Modified Organism) (Hanif, 2014). Often deficiencies and defects in a type of product are used as a basis for distrust from outside products, especially for specific countries, causing a ban on entry of all similar products from that country into the domestic market. Although there are no general health standards agreed upon by all countries that cause the elimination of certain products, this causes the creation of obstacles in free and fair trade.

Another form is the anti-dumping policy. This policy explicitly aimed at avoiding other predatory trade policies of the domestic market and world trade. Dumping policy is carried out by applying subsidies that are very large for domestic products to compete in the global market at prices far below production costs. This matter is considered to have to be responded directly because the country that applies this policy aims to be able to dominate the world market monopolistic.

The anti-dumping policy is a legitimate policy when it is aimed at avoiding world market domination by fraudulent means by one country. However, the accusation that other countries are implementing dumping policies is often used as an excuse in the application of anti-dumping policies that discriminate against outside products even though they have a comparative advantage in producing a commodity effectively. This kind of policy is tantamount to giving distrust to the policies applied by other parties. Anti-dumping can cause more severe impacts than tariffs because they tend to be less transparent.

Third, **instrumental protectionism**, this form of protectionism is the least transparent and applied form by using trade policy as a tool to encourage political policy change in other countries. If the bluff given is successful in changing the policies of other countries, the protectionist policy does not become applied, although it positively influences the political relations between the countries. However, if there is no political change, a form of trade protection will be applied as a consequence of the threat.

This method has been carried out by the United States by threatening to exit the North America Free Trade Area (NAFTA) agreement if its member

countries do not want to incorporate aspects of labor and environmental welfare into the mechanism of trade agreements (Hanif, 2014). This snapping prompted countries in North America to reform some of their trade policies. The same thing was also taught by the United States in the framework of the WTO but was rejected by the majority of developing countries because it was difficult for peacocks to adopt aspects of labor and environmental welfare shortly. The refusal of the majority of WTO member countries ultimately did not cause the United States to implement a protectionist policy towards developing countries. The factor of political balance is one of the considerations in applying this type of protection.

D. Hypothesis

From the background of the problem and the basic framework of thought or theory described above, the reason why does the European Union decide to ban the import of Crude Palm Oil for the use of biofuel in 2020 is:

The European Union seeks to support renewable energy and improve economic welfare in an effort to protect domestic companies, especially in the biofuel industry by making domestic products produced by European farmers become the main energy sources previously sourced from imported crude palm oil (CPO).

E. Scope of Research

The complexity of trade relations between Indonesia and the European Union, especially for CPO, the authors limit the scope of research from 2010,

precisely after the achievement of Partnership and Cooperation Agreement (PCA) until 2018 where the European Union decided to end CPO imports.

F. The Aim of Research

The aim of this scientific research are:

- a. Explain the reasons for the European Union which have set 2020 as the deadline for banning the import of Crude Palm Oil intended for conversion into biofuel.
- b. I am completing the final assignment of study in the International Relations Program, Faculty of Social and Political Sciences, Universitas Muhammadiyah Yogyakarta.

G. Methodology Tools

- a. Tool of Analysis
Based on the object of analysis, the tool of analysis of this study is international trade regarding relations and trade agreements between Indonesia and the European Union.
- b. Kind of Research and Data
The of the research is qualitative, the research using an approach with a broad range of domains, with the aim of making descriptions, systematic and accurate explanations and descriptions related to facts, characteristics and relationships analyzed. Data collected is secondary data or data arranged in an indirect form.

- c. The technique of collecting data
In the preparation of this thesis, the collecting data technique used by the author is the library research. With this technique, the authors hope to find data or facts that are relevant to the problem under the research. The library research that the author use comes from various literature related to research in the form of books, scientific journals, newspapers, media reports, government policies as well as articles that related to the object of research.
- d. Method of analysis
The method of analysis used by the author to analyze this research is a descriptive or explanatory method.

H. System of Writing

The systematics of writing this thesis consists of four chapters, and each chapter will contain the following:

- CHAPTER I** This is introduction chapter, the author describes the background of the problem, the research question, the theoretical framework, the hypothesis, the scope of research, the aim of the research, the methodology tools and finally the system of writing.
- CHAPTER II** This chapter contains a description of the background of trade relations between Indonesia and

the European Union, the principles or economic systems of each country, and the forms of cooperation that already established between Indonesia and the European Union.

CHAPTER III This chapter describes the causes of deteriorating trade relations between Indonesia and the European Union, and indications or determinants of trade policy between Indonesia and the European Union.

CHAPTER IV This chapter is a closing that contains the author's conclusions from the results of the discussion contained in chapter I to chapter III.