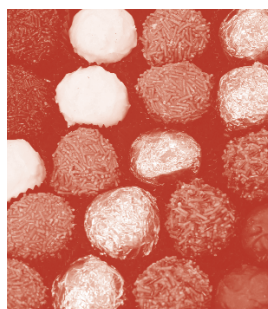


# Investment Guide to the **INDONESIAN** Food and Agriculture Sector



Prepared for the  
Australian Government Department of Agriculture,  
Fisheries and Forestry

by **Bayliss Associates Pty Ltd**

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#### **Disclaimer**

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## FOREWORD

**Since the December 2004 tsunami devastation, the relationship between Australia and Indonesia has strengthened. Indonesian President Susilo Bambang Yudhoyono has urged Australian businesses to increase investment in Indonesia and singled out food processing and beverage manufacturing as an area of opportunity.**

In their Joint Declaration on a Comprehensive Partnership between Australia and Indonesia, signed in April 2005, Prime Minister Howard and President Yudhoyono noted that Australia and Indonesia share a fundamental commitment to economic growth and development.

There is increased optimism about Indonesia's economic future, with average incomes returning to levels experienced prior to the financial crisis of 1997. Agrifood has made a significant contribution to Indonesia's GDP, growing at 4.5% per annum over the past decade.

Urban populations are expanding rapidly, incomes are increasing and more women are entering the workforce. Modern retail outlets, increasing consumer sophistication, growing health consciousness and interest in new foods are currently driving sales.

Indonesia and Australia have complementary economic strengths. Differences in resource endowments, production technologies and consumption patterns present numerous opportunities to encourage trade and agribusiness investment.

Australia is a substantial exporter of agrifood products to Indonesia and maintains a very active development assistance program in agribusinesses. However, Australian companies have only invested in a limited way in agrifood production and processing in Indonesia. The time has come, we believe, for a new stage of closer engagement that includes greater bilateral trade in agrifood and more direct foreign investment.

This guide provides information for identifying new investment opportunities in the Indonesian food and agriculture sector. It was commissioned by the Working Group on Agriculture and Food Cooperation and the Working Group on Trade, Industry and Investment. These Working Groups operate under the auspices of the Australia-Indonesia Ministerial Forum. Their overall purpose is to strengthen cooperation between Australia and Indonesia in order to develop commercial linkages.

We recommend the guide to those looking for investment opportunities and seeking a better understanding of the future growth potential of the Indonesian food and agriculture sector.



**The Hon Peter McGauran MP**  
Australian Government  
Minister for Agriculture, Fisheries and Forestry



**H.E. Dr Anton Apriyantono**  
Republic of Indonesia  
Minister for Agriculture

August 2005



## EXECUTIVE SUMMARY

Renewed capital investment is a cornerstone of development for the new government of Indonesia's President Susilo Bambang Yudhoyono<sup>1</sup>, and fresh efforts are underway to redress the structural impediments that have slowed that investment in the past. No sectors are more important to the President than food and agriculture development and there is strong encouragement from both the Australian and Indonesian Governments for Australian agrifood-related<sup>2</sup> companies to review Indonesian investment opportunities which are a natural fit with Australian capability.

- Indonesia offers a market base of some 220 million consumers, with GDP currently growing at a rate of 5.4% per year.<sup>3</sup>
- Australian food and beverages are particularly well-recognised in Indonesia and enjoy favoured positioning in the market.
- There is strong complementarity between the food and beverages Australia produces and Indonesian consumers demand.
- The latest data on investment approvals in Indonesia demonstrate an improved investment outlook. After falling more than one-third to US\$10.28 billion in 2004, foreign direct investment approvals in the first three months of 2005 were US\$4.28 billion – an increase of 173% over the same period in 2004.<sup>4</sup> Recent reports also indicate that domestic investment is on the rise.<sup>5</sup>
- The Australia-Indonesia business climate is positive and there is a growing awareness that the Indonesian economy is now back on track.
- From the perspective of an Australian investor, the dollar to Indonesian rupiah exchange rate is currently at an historically very favourable level.

Indonesian firms contacted for the preparation of this Guide expressed solid interest in working with Australian companies. Australian agrifood expertise is well-recognised and, combined with Australia's reputation as an exporter of quality food products, provides a strong basis for new business engagements.

This *Investment Guide to the Indonesian Food and Agriculture Sector* focuses on ten market sectors and profiles opportunities in these sectors. It is a précis of a much larger *Report on Investment in the Indonesian Food and Agriculture Sector*, which provides additional background on the sector and information on investment procedures and regulations in Indonesia. The Report can be accessed on the website of the Australian Government Department of Agriculture, Fisheries and Forestry (DAFF).<sup>6</sup> Both the Guide and Report examine the techniques Australian and Indonesian companies have adopted to create successful new business.

The Guide also provides an appendix of contacts including trade and industry associations, government agencies, business advisers, lawyers and accountants and other helpful sources of advice and information, including a listing of websites available for further reference.

<sup>1</sup> Popularly known as SBY.

<sup>2</sup> The terminology 'agrifood' is defined in the 'Scope of the Guide' on the following page and in the Glossary of Terms.

<sup>3</sup> Economist Intelligence Unit – Quarterly Economic Survey, 22 March 2005.

<sup>4</sup> BKPM – Indonesian Capital Investment Board.

<sup>5</sup> New York Times, 18 February 2005.

<sup>6</sup> <http://www.daff.gov.au/foodinfo>.

# INTRODUCTION

**President Susilo Bambang Yudhoyono and Prime Minister John Howard have both identified renewed investment in Indonesia as key to economic recovery and development. The President sees agrifood as a critical growth sector.**

**Indonesia, with a population in excess of some 220 million people, is the world's fourth largest country. Its population growth rate exceeds that of China, India and the USA, and it is one of the world's major agrifood markets.**

Despite exports of over A\$320 million<sup>7</sup> in agrifood products to Indonesia in 2004, Australian investment in Indonesian agrifood industries remains extremely low. This situation is not unique as the level of Australian investment overall in Asia is also disproportionately low in comparison with merchandise trade.

There is concern that Australia's low level of investment could come at a cost to long-term market development. As the Reserve Bank of Australia Governor, Mr Ian MacFarlane noted in March 2005, 'One of the major characteristics of the development of Asia over the past decade has been the increase in cross-border interdependence of production.'<sup>8</sup> Implicit in this cross-border interdependence is the need to back export performance with strategic investments.

Both the Australian and Indonesian Governments recognise the need to encourage new investment in Indonesia – and there is no sector more vital than that of agrifood development.

Following the inauguration of President Susilo Bambang Yudhoyono, there are signs that the Indonesian economy is once again gaining direction and momentum, and the government has begun to tackle governance issues that have inhibited investment in the past.

This Guide to investment in the Indonesian food and agriculture sector is an initiative of the Australian and Indonesian Governments. It has been produced under the auspices of the *Working Group on Agriculture and Food Cooperation (WG AFC)* and the *Working Group on Trade, Industry and Investment (WGTII)* and is a summary of a larger Report on Investment in the Indonesian Food and Agriculture Sector that is available on the website of the Australian Government Department of Agriculture, Fisheries and Forestry (DAFF).<sup>9</sup>

The Guide and its companion Report also complement The Food Exporters' Guide to Indonesia (2004) prepared by Instate Pty Ltd.<sup>10</sup> Further detailed analysis is provided in the publications prepared by the Australian Government Department of Foreign Affairs and Trade (DFAT) in the *Subsistence to Supermarket II* Project series.<sup>11</sup>

## SCOPE OF THE GUIDE

The Guide reviews Indonesia's attractiveness as a foreign investment destination in the broadest sense. It examines green field, as well as other investment models for the agrifood sector, including:

- mergers and acquisitions
- multi-partner investments with third countries
- licensing and technology agreements
- brand-building and marketing arrangements.

**This Guide provides a practical roadmap to help Australian companies develop agrifood investment opportunities in Indonesia.**

<sup>7</sup> This figure excludes wheat exports from Australia to Indonesia, which are classified as Confidential Items.

<sup>8</sup> Australian Financial Review, 31 March 2005.

<sup>9</sup> <http://www.daff.gov.au/foodinfo>.

<sup>10</sup> Also available on the above website.

<sup>11</sup> Available for purchase through the DFAT website <http://www.dfat.gov.au/publications/agrifoodasia>.

Throughout the Guide the terminology ‘agrifood’ is used to refer to the full spectrum of the food and agricultural sectors, and includes any food or beverage product, or ingredient in a food or beverage product, from the raw and unprocessed state to that of a highly processed finished product.<sup>12</sup>

In the same context the term agrifood-related companies covers all companies involved in any stage of the production, processing, distribution and/or sale of agrifood, whether by provision of goods and/or services.<sup>13</sup>

## METHODOLOGY

This Guide has been developed to identify areas of natural fit between Indonesian market potential and Australian investment capability. After consideration of the broad scope of the Indonesian agrifood sector, ten areas were chosen for further analysis as being the most prospective for Australian investment. These areas are:

- fruit and vegetables
- dairy
- beverages
- poultry
- beef
- bakery products
- confectionery
- snack and convenience foods
- baby foods
- food ingredients.

Opportunities in each of these ten sectors were assessed directly from interviews with Australian and Indonesian companies, and were analysed against Australian, Indonesian and global market settings. Key considerations were:

- growth potential
- scale of operation
- foreign investment
- competitive pressures
- perceived Australian advantage.

In each of the sectors, investment attractiveness was also tested against the following criteria:

- ease of entry
- capital requirement
- sales potential.

<sup>12</sup> It is taken directly from the DFAT publication ‘Agrifood Globalisation and Asia’, part of the Subsistence to Supermarket II Project series, referenced previously.

<sup>13</sup> Op. cit.

To provide coverage of these issues and to assist the process of investment identification, the Guide is divided into four parts:

**Part One: Overview.** This section provides a brief review of Indonesia's agrifood potential and Australia's existing investment activity in this sector. It also provides a synopsis of the findings and a ranking of the ten sectors identified in terms of investment attractiveness.

**Part Two: The Investment Assessment Process.** This part provides a checklist of important considerations in the investment process. It offers a step-by-step analysis of issues involved and lays out a general roadmap of investment procedures in Indonesia.

**Part Three: Areas of Investment Opportunity.** Following a brief commentary on the characteristics of the Indonesian food sector, this part of the Guide looks more deeply at the ten sectors identified as offering opportunities.

**Part Four: Tips and Recommendations.** This section offers suggestions of where to go for advice and assistance and how to structure an investment evaluation strategy. Supplementary information is provided in Appendices C and D of the Guide.

## PART ONE: OVERVIEW

### INDONESIA'S AGRIFOOD POTENTIAL

In population terms Indonesia is the fourth largest market in the world, after China, India and the USA. Its population is growing faster than in these other markets, yet in investment terms, Indonesia has been 'off the screen' since the late 1990s for most international and Australian agrifood-related companies.

Foreign direct investment (FDI) in agrifood businesses has literally poured into China in the last seven years, and risen substantially in India and the USA. In Indonesia over the same period there has been a net capital outflow.<sup>14</sup> There are now signs, however, that the market is recovering – and companies seeking a preferred position for the longer term are well-advised to take a fresh look at Indonesian investment options.

Many multinational groups and regional Asian companies, particularly from Singapore and Malaysia, see the current circumstances as particularly favourable to investment. While there are inevitably risks early in a recovery cycle, and while Indonesia still has a range of governance issues to resolve, current exchange rates are particularly favourable in restraining set-up costs. Good market openings exist and some Australian companies are developing them. The new *Indonesian Investment Act* to be introduced in 2005 will help to simplify investment procedures.

- The agriculture sector in Indonesia is, however, sensitive to foreign investment. Complex issues of smallholder communities, land ownership, cooperative marketing and a long history of government intervention mandates a well-considered, long-term strategy.
- The food processing sector is less complex, although local raw material supply can be problematic.

Indonesia's vast archipelago of 16,000 islands presents challenges for production and distribution. Greater Jakarta is the major market for foodstuffs and Java is the centre for most food production.

The outer islands provide competitive agricultural land and low-cost labour, but communication and transport costs are considerably higher. To succeed in these markets, investors need to harness productive resources with efficient manufacturing and innovative marketing techniques.

Plantation and estate production of commodities (such as palm oil, cocoa, coffee, rubber, spices, vanilla and tea) has been generally successful as a result of economies of scale and modern processing techniques. This sector is dominated by Indonesian and foreign (usually Malaysian) conglomerates. Market entry to this sector is best approached by an alliance with an existing producer.

#### The dominance of Java in food processing.

Figure 1 demonstrates the concentration of food processing activity in Java. Each dot on the map represents a food processing factory employing more than 500 staff. The other major manufacturing centres are North Sumatra, South Sumatra and North and South Sulawesi.

***'We need to unlock the potential of 200 million consumers to the north of Australia. After China, Indonesia is the most exciting and promising growth play for Australian agrifood companies.'***

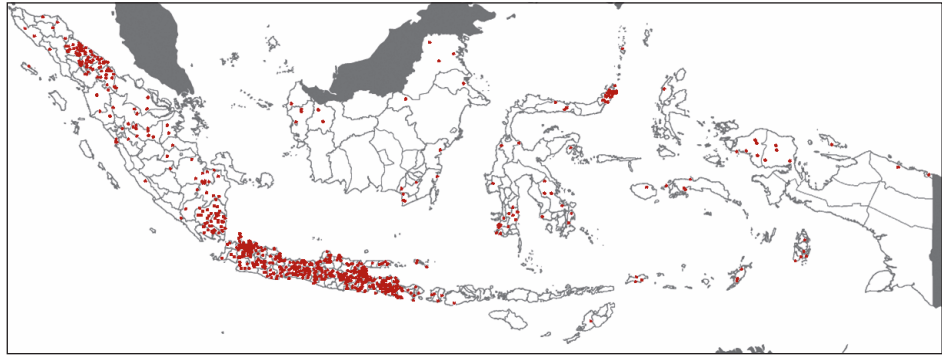
Leading Australian agrifood executive

***'The timing is right for Australian companies to reassess Indonesia's investment potential. The economy is on an uptick and Indonesian equity markets are strong.'***

Australian CEO

<sup>14</sup> For a full review of the background of Indonesia's investment climate since 1997, please refer to the full report mentioned previously as available on the DAFF website.

Figure 1: **DISTRIBUTION OF FOOD PROCESSING IN INDONESIA**



Source: World Bank Investment Study, December 2004

## **AUSTRALIAN INVESTMENT EXPERIENCE**

Australian investment in Indonesian agrifood industries has been modest compared with that in mining and secondary industries, such as building and construction. A factor in this has been that Australian agrifood companies have also been prime targets for foreign investment, and overseas-owned companies dominate in areas like food processing. In Australia this trend in foreign acquisition of agrifood assets shows no signs of abating.

In grains, meat and dairy, Australian companies are large exporters to Indonesia, and are well-experienced and embedded in the market. On the ground investment is, however, relatively limited. Some examples of Australian agrifood presence:

- Arnott's manufactures biscuits in Indonesia.
- AustAsia subsidiary, PT Greenfields, has an integrated dairy operation in East Java.
- The Berri group has a joint venture in Indonesia producing fruit juices. San Miguel of the Philippines recently took a 50% stake in Berri and has announced that the two companies will work together to expand beverage production in Indonesia.
- Cheetham Salt has refining facilities in West Java.
- Coca-Cola Amatil is the principal Coca-Cola licensee in Indonesia.
- Davids Logistics Services has large warehousing facilities just outside Jakarta, and have been directly involved in food distribution with a major supermarket group.
- Goodman Fielder (Meadow Lea margarine) has a joint venture with the PT Sinar Mas conglomerate.
- KH Foods (formerly Keith Harris & Co.) has a joint venture in the production of flavourings.
- Linfox has logistics operations in Jakarta and works with key clients including Unilever.
- Manildra Milling has a presence in Jakarta, Surabaya and Medan.
- Nandos Australia has restaurant franchise operations in Bali and Jakarta.

Multinational corporations (MNCs) such as Mars, McDonald's and Simplot use Australia as a regional source of production inputs, and draw on a variety of Australian managerial resources for their offshore operations in Indonesia and the South East Asian region.

## **RANKING INVESTMENT ATTRACTIVENESS**

Investment prospectivity is not easily quantified. Subjective perceptions inevitably influence the decision process. In this study investment attractiveness has been assessed in the first instance on a *green field* investment basis and the rankings were then qualified by comparison with alternative investment strategies, and a range of investment alternatives for a practical blend of investment entry models.

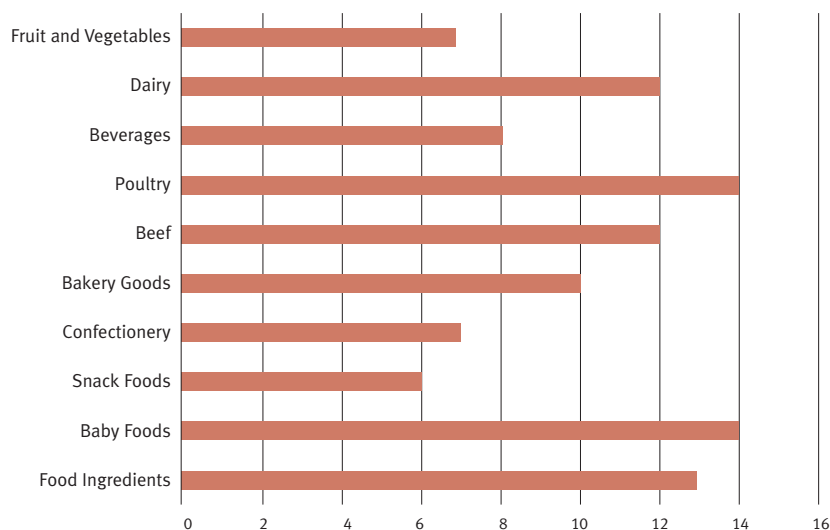
***Many Australian companies have been content to export, waiting to be convinced that investment will yield a better return. There are clear indications that this re-examination is now timely.***

For example, the un-moderated ranking of investment attractiveness for the beef sector is low in this analysis. The assessment is based on high market entry costs, strong competition and long lead times required to attain profitability.

The purchase of an existing beef feedlot and processing operation could, however, substantially lower entry hurdles, but it is difficult to factor such an acquisition into a quantitative ranking in view of the scarcity of suitable operations.

The following graph indicates relative growth potential for the ten primary sectors assessed in the study. The growth assessments were determined by consolidating industry comments and applying reliable market growth forecasts, where available.

Figure 2: **THE GROWTH POTENTIAL OF KEY AGRIFOOD SECTORS % VOLUME (2005–2006)**



## THE FINDINGS

The following two tables outline the rankings of Indonesian agrifood sectors for:

- industry characteristics
- investment attractiveness.

These indicators require moderation and analysis which is provided in the ‘*Attractiveness Ranking*’ graphic (see Figure 3).

Table 1: **INDONESIAN FOOD INDUSTRY CHARACTERISTICS (SCALE 1=LOW 10=HIGH)**

INDUSTRY SECTOR	SCALE OF OPERATION	FOREIGN INVESTMENT	COMPETITIVE PRESSURES	AUSTRALIAN ADVANTAGE
Fruit and Vegetables	7	3	4	4
Dairy	5	7	6	8
Beverages	7	6	8	6
Poultry	5	5	7	2
Beef	4	6	5	8
Bakery Goods	8	4	8	6
Confectionery	7	5	8	4
Snack Foods	7	5	7	3
Baby Foods	8	8	8	3
Food Ingredients	4	4	6	7

Table 2: **INVESTMENT ATTRACTIVENESS MATRIX (SCALE 1=LOW 10=HIGH)**

INDUSTRY SECTOR	EASE OF ENTRY WEIGHTING 0.4	CAPITAL REQUIREMENT WEIGHTING 0.3	SALES POTENTIAL WEIGHTING 0.3	OVERALL ATTRACTIVENESS
Fruit and Vegetables	3	5	5	4.2
Dairy	4	6	7	5.7
Beverages	4	6	7	5.7
Poultry	2	6	7	4.7
Beef	3	5	5	4.2
Bakery Goods	6	4	6	5.4
Confectionery	6	4	6	5.4
Snack Foods	6	4	7	5.7
Baby Foods	2	2	7	3.5
Food Ingredients	5	7	7	6.2

Tables 1 and 2 and Figure 3 provide a schematic presentation of investment opportunities for each of the ten sectors that have been examined. The ratings do not represent a precision measurement, but they are an attempt to provide a basic template for the prioritisation of sectors in investment terms. They are drawn from extensive interviews and sector analyses, and devised primarily to assist in identifying market entry hurdles.

The relative rankings of investment attractiveness which appear in Figure 3 need to be read in association with the more detailed assessment of the individual ten market areas which appear in Part Three of this Guide.

It is naturally unlikely that prospective investors would consider commitments beyond their core activity areas, and hence there is no suggestion that individual investors would look for engagement beyond one or two of the ten areas identified. The relative rating of these ten key areas, however, has been provided to offer a perspective of the degrees of opportunity and challenge that individual Australian investors could encounter across the agrifood sector in Indonesia.

Figure 3: **INVESTMENT ATTRACTIVENESS RANKING**

<b>Food Ingredients</b> →	New opportunities emerging where Australia has a strong advantage.
<b>Snack Foods</b> →	Prospects for working with Indonesian producers on new brands.
<b>Confectionery</b> →	A highly fragmented industry where niche opportunities exist.
<b>Beverages</b> →	A range of opportunities where Australian innovation could provide competitive edge.
<b>Dairy</b> →	Australia has supply capabilities and should be positioned for greater engagement.
<b>Poultry</b> →	Few Australian players. Excellent long-term potential in view of dietary protein needs.
<b>Bakery Goods</b> →	High growth and potential in ingredients.
<b>Fruit and Vegetables</b> →	Much potential, but raw material supply and handling a major issue.
<b>Beef</b> →	Potential for derivative products – but barriers to entry now high.
<b>Baby Foods</b> →	Strong MNC competition but prospects for infant food.

## PART TWO: THE INVESTMENT ASSESSMENT PROCESS

### Step 1: MARKET PROSPECTS

Investment requires a deeper understanding of the structure and characteristics of a market compared with general merchandise trade. A company that has been trading successfully in Indonesia for many years, no matter how familiar they consider they are with the way business is done, should seek further specialist advice before investing.

The following is a suggested strategy for investment evaluation:

- **First identify and study existing publicly available research material on your industry and your specific market in Indonesia.**
- **Armed with this level of information, identify the best professional research that is available for purchase.**
- **Use government and business agencies (such as Austrade,<sup>15</sup> DFAT<sup>16</sup> and the AIBC<sup>17</sup>) to develop a comprehensive assessment of market data available.**
- **Consult with EFIC<sup>18</sup> concerning risk evaluation.**
- **Ensure you are fully across this desk research before visiting the market to assess investment options – as understanding this background will better inform your on-the-ground observations.**
- **Use Austrade and other government and business agencies to prepare your visit program and for a briefing on market conditions.**
- **Talk to your Australian bank. Australian banks, particularly the ANZ and Commonwealth Bank, are well-connected in the Indonesian market. Rabobank is also well-positioned in agrifood.**
- **Pay particular attention to what your domestically based competitors (Indonesian and multinational) are doing in Indonesia.**
- **Research potential business partners in depth before face-to-face contact.**
- **Take a hard-headed view of prospects and challenge all optimistic projections made by those who have a vested interest in the investment.**

*The Indonesian agrifood market is on the cusp of change. Understanding Indonesian consumer behaviour, before and after the financial crisis of 1997/98, is imperative in structuring business models for the future.*

The following check list addresses some of the basic business issues that need to be considered when developing a strategy for investment in Indonesia. The following advice does assume some prior familiarity with the Indonesian market.

Individuals who have a limited knowledge of the Indonesian trading environment are recommended first to read the publication *Food Exporters' Guide to Indonesia*.<sup>19</sup>

<sup>15</sup> The Australian Trade Commission <http://www.austrade.gov.au>.

<sup>16</sup> Op. cit. <http://www.dfat.gov.au/publications/agrifoodasia>.

<sup>17</sup> Australia Indonesia Business Council <http://www.aibc.com.au/>.

<sup>18</sup> Australian Government Export Finance and Insurance Corporation <http://www.efic.gov.au>.

<sup>19</sup> Op. cit. <http://www.daff.gov.au>.

## CHECKLIST FOR ASSESSING MARKET PROSPECTS

ISSUE	HOW TO DO IT	RESULTS
What is the advantage of manufacturing my product, or delivering my service in-market rather than exporting direct from Australia?	<p>While still in Australia, assess how your prime domestic and foreign competitors are positioning themselves in Indonesia. Use Austrade and/or a business consultant with well-established links in Indonesia and talk to other companies that have a presence in the Indonesian market.</p> <p>Attend networking functions held by the AIBC, Chambers of Commerce, DFAT, Austrade and state governments.</p>	<p>Learn from the experience of others.</p> <p>This approach will help ensure you ask the right questions to make an accurate market analysis.</p> <p>It enables you to assess more effectively the proposals that your Indonesian associates, business partners, clients and customers are making. It also helps you to begin calculating the costs and benefits of direct investment.</p>
A SWOT analysis	<p>Obtain price surveys from buyers and Austrade.</p> <p>Detailed assessment of offshore and onshore competition.</p>	Time spent in researching competition may save many expensive visits and negotiations.
Assess the nature and scale of the business engagement required – from a representative office to a more complex business arrangement	<p>Deeper discussions with Indonesian end-users, intermediaries and consultants.</p> <p>Rigorous analysis of establishment costs.</p>	Decide whether your company needs a ‘bricks and mortar’ type presence or whether the market is best serviced by direct exports or a trading office facility.
Identify the ‘big issues’	<p>Talk to companies that are successful in the market. Try to determine why they succeeded and seek anecdotal data on why others have failed.</p> <p>The lessons of failure are often as important as the clues to success.</p>	<p>Focus on and prioritise the major factors needed for success – and their costs to acquire.</p> <p>This approach provides clearer vision for overall business planning and cost analysis.</p>
What type of business structure is best suited to developing the Indonesian market for my product/service?	<p>Approach legal and accounting firms, as well as business consultants and advisers who have the best track record in your market sector.</p> <p>Endeavour to ensure their advice is impartial.</p>	<p>Assess consultants’ advice against your objectives and benchmark against costs/benefits of a similar scale investment in your home market and alternative offshore locations.</p> <p>Factor in the value of a geographic spread of investments to cushion cyclical business trends in Australia and other markets.</p>
Contingency planning	Approximate or model possible changes in key variables (e.g. exchange rate movements, political risk, commercial risk, ‘left field’ factors [e.g. bird flu outbreak]), and consider possible impacts and responses to minimise negative effects.	This will improve your ability to weather any nasty shocks or surprises that the market may throw up.
Create a business plan	Develop realistic timelines, validating them with the advice of those familiar with the process, rather than promoters of investment who will present an optimistic view.	Calculate return on investment parameters and identify project milestones in the business establishment process.

## Step 2: FINDING THE RIGHT LOCAL INVESTMENT PARTNER

Partner searches are usually the most critical – and most difficult – aspect of establishing an offshore business. There are no rules that guarantee success.

### Key considerations:

- **Take your time. Rash decisions can set back business development for years.**
- **Use a structured business process for partner analysis.**
- **Develop a financial plan early and assume that results will take considerable time to achieve.**
- **Get good advice on legal and financial issues.**
- **Seek advice from other Australian companies and Australian government and state agencies that have a presence in the Indonesian market.**

*'I want partners with good connections. I also need someone who understands the dynamics of my industry and has a vested interest in ensuring a project will work.'*

Australian CEO

Some companies have been successful in identifying their local partners or associates on first meeting. Long-term experience indicates that a carefully planned, analytical process substantially reduces the risks associated with partner selection. As with marriage – the golden rule is *don't rush into it*. Here are some suggested guidelines:

### A PARTNER SEARCH CHECKLIST

HOW TO DO IT	THE PROCESS
Develop a profile of your 'ideal' partner. Leave the 'chemistry' till later.	Assess financial and management resources, manufacturing capability, distribution reach and technical support.
Conduct extensive desk research before setting foot in the market.  The internet delivers huge productivity gains.	Buy market research reports on your industry sector in Indonesia. There are generally good, reputable ones available.  Many research companies sell reports by segment and this will reduce costs, enabling you to buy only what you need.
Assemble a list of prospective partners using Austrade, business consultants and by networking. Cross check with other contacts, including if possible some current and past business partners and/or suppliers and customers. Rigorously check out any potential conflict of interest.	First hand referrals from Australian companies in related fields can be very valuable.
Plan a structured business visit with as many confirmed meetings as possible.  Blend advice from a variety of sources to gain a 'whole of market' view, not just the perspective from a distributor or agent.  Keep a broad perspective and avoid premature commitments.	Take a vertical 'slice' of the market and meet contacts from government, chambers, industry associations, end-users, manufacturers, wholesalers, agents, advisers and consultants.  Use Austrade, state governments and/or consultants to fix meetings. Arrange meetings directly wherever possible for maximum impact.
Develop a short list of potential business partners, with high weighting on industry referrals and evidence of track record.	Undertake credit and other background checks on prospective partners, and contact other foreign companies they are associated with.
Consider inviting potential partners to Australia to judge their 'fit' with your operations, your associates and business advisers.	Austrade's Export Market Development Grants (EMDG) scheme may assist with the costs of these visits.

Foreign companies that have been successful in Indonesia overwhelmingly stress the importance of an effective local partner or associate. Even companies that are wholly owned subsidiaries of foreign companies develop relationships with distributors and other forms of commercial alliances. These can prove invaluable in negotiating one's way through an often opaque trading environment.

Time spent at the identification and selection stage pays huge dividends. The costs of an inappropriate or failed partnership are huge and most likely will compromise the success of the venture. The Indonesian legal process tends to favour the local company and litigation can be expensive, time-consuming and often inconclusive.

### Step 3: FORMING A BUSINESS ENTITY IN INDONESIA

There is an increasing range of choices for establishing a business structure in Indonesia. Many of these are not as expensive as a traditional joint venture (JV) operation.

- **Increasing liberalisation of the Indonesian business environment has opened opportunities for innovative business linkages.**
- **Choose an adviser with proven experience and a strong local presence.**
- **Seek support from Australian and Indonesian government agencies.**

Some of these options are listed in the following table, along with comments concerning their suitability for various business models.

Table 3: BUSINESS MODEL OPTIONS

BUSINESS STRUCTURE	FEATURES AND BENEFITS	COMMENTARY
Joint Venture Company	This is the most common model for South East Asian investment – principally because of various controls on the degree of foreign ownership. Controls are now easing, and a number of models are emerging. The bottom line for overall success of a venture, however, tends to be ‘cultural fit’ with the local partner and their overall capability and inclination to contribute to the success of the venture. There are many advantages in a JV structure, but a key consideration is the ability to navigate through the local bureaucracy and ‘getting things done.’ Access to the partner’s distribution network is also frequently a critical factor in JVs.	Joint ventures will continue to be the favoured business model for many major manufacturing operations. Identification and selection of a partner is critical and should be undertaken in a well-considered and deliberate fashion, although in some industries a ‘natural partner’ is evident.
100% Foreign-owned Company	This is a more recent option available through further deregulation. It has been successfully used by a number of companies. It has the advantage of independence in decision-making – but it does not provide for the local insights of a JV partner. The corporate structure is simple and offers flexibility in adapting to market conditions.	Successful models often include non-equity alliances with local companies who have a strategic stake in the business (e.g. contract manufacture, distribution and marketing). These can provide a level of ‘insider’ advice that the JV partner would normally deliver.

Table 3: **BUSINESS MODEL OPTIONS** (cont.)

<b>BUSINESS STRUCTURE</b>	<b>FEATURES AND BENEFITS</b>	<b>COMMENTARY</b>
<b>Acquisitions</b>	Indonesia's mergers and acquisition (M&A) boom of 1998–2001 is over. During that period following the financial crisis of 1997/98 <sup>20</sup> , many foreign companies purchased very competitively priced assets. While purchase prices are now higher, the ability to inject strong brands and technology into existing Indonesian companies continue to attract foreign investors towards either full or part acquisition.	As the Indonesian economy opens more to global forces, attractive M&A prospects will continue to appear, although the previously high levels of distressed sales have diminished. In the food sector, there are Indonesian companies which would benefit from a foreign shareholder. Many of these, however, are family-controlled and operating in a family management environment presents particular challenges. Historically low exchange rates with the Australian and US dollars continue to facilitate acquisition.
<b>Licenses and Technical Associations</b>	The deregulated Indonesian environment now offers considerably more opportunities for non-equity business alliances, notably in the retail and distribution sectors, as well as franchises. Financial risks are low but careful attention must be paid to brand protection and product and/or service quality assurance.	The choice of business partner is critical as these arrangements rely heavily on a high degree of trust in view of variable legal and policy settings. Well-regarded legal and financial advisory services are available to develop business structures of this nature.
<b>Commercial Agreements</b>	This category covers a wide range of business associations which do not involve equity, but bind companies in commercial agreements that are outside the traditional 'agent/principal' model of import/export trade.	Australian legal and financial advisory firms can suggest a range of business models tailored to specific commercial circumstances.
<b>Third Country Associations</b>	Investment engagement in Indonesia from Singapore and Malaysia is high. Locating Singaporean and Malaysian (and other Asian) companies whose interests are complementary can provide a highly effective market entry model, which builds on the experience of the other parties. Time spent in searching out potential business associates in South East Asia can prove highly profitable (Appendix B provides further specific information on the Singapore scenario).	A range of engagements is possible, from a buy-in to a technical or commercial association. Most importantly, Australian companies may find it useful to seek out alliances of this nature, rather than taking an Indonesia-only approach, particularly when planning to build a regional marketing base. South East Asian companies are well-embedded in Indonesia and are increasing their investment presence.
<b>Australian Associations</b>	There is nothing new about 'piggy back' arrangements with other Australian companies where their experience is complementary. These types of associations are more prevalent in remote and 'difficult' markets, but the model is equally valid in Indonesia.	Finding the right partner and the correct 'fit' is never easy, but Australian companies often 'go it alone' without researching potential alliances with other Australian companies – even competitors – but where business interests can be complementary. These types of arrangements can also deliver significant cost savings, particularly during the critical start-up period.

<sup>20</sup> This period of financial crisis is known commonly in Indonesia as 'krismon' or the monetary crisis.

***‘Establishing a manufacturing operation in Indonesia with core ingredients from Australia, means our company can get access to food processors servicing high volume markets.’***

Leading Australian producer

## LEVELS OF REPRESENTATION

When considering the business model and level of investment to adopt, a particular issue is often whether to appoint an expatriate manager or not. For small to medium size enterprises (SMEs), expatriate packages can be an expensive option, but generally provide a higher measure of management control. They can be the preferred option, especially during the establishment phase, but there are also other less costly alternatives, such as contracting the services of a locally based consultant to oversee the company’s interests and provide on-the-ground monitoring capability.

Options must be considered carefully, particularly in relation to the size and expected return on the investment. There are no fixed and fast formulas that can be applied.

Regular visits from key Australia-based executives are nevertheless critical to ensure the new investment meets the operational guidelines and quality control standards that are expected.

If expatriate representation is essential to establish a company’s presence and ensure that work practices and standards reflect those of the parent company, there are a range of options to consider. With careful attention to structuring salary packages, as well as arrangements for accommodation and transport etc., reasonable and performance-based provisions can be made. The major accounting firms are well-experienced in providing this type of detailed advice on the options available.

## LICENSING

As another alternative, many companies choose to license their products and services in Indonesia to avoid the cost and time to establish a local operation and to avoid the complexities of operating in a foreign tax regime. This mode of entry often has appeal to SMEs when both financial and human resources are limited.

While this option has many attractions, it does require that particular care is given to the selection of a local associate. There are many examples of highly successful licensing structures, and the food franchise sector is one area where a number of Australian companies have followed this route.

Sound local legal advice is necessary in the establishment of agreements and contracts. Fortunately, there is a great deal of experience to call on when framing these arrangements.

Protection of intellectual property (IP) in Indonesia can be both difficult and expensive, and establishing high levels of trust with an Indonesian business partner is critical in arrangements of this nature. As noted previously in other areas of litigation, bringing IP disputes before the local courts can be both costly and time-consuming, and may not be successful.

## FRANCHISES

Many of the world’s major fast food providers commenced operations in Indonesia in the 1980s and enjoyed buoyant trading conditions until the 1997/98 financial crisis. The severe downturn in the Indonesian economy that followed resulted in a significant rationalisation of the industry. A number of groups, including McDonald’s, adapted their offerings to these depressed conditions, with smaller size servings as well as ‘crisis’ products (such as egg and rice) as a way of trading through until recovery.

Western fast food is now a well-established feature of the Indonesian food scene with global brands such as McDonald’s, Kentucky Fried Chicken (KFC) and Pizza Hut represented in all major cities. They are particularly evident in modern shopping centres and malls.

Starbucks has made inroads, catering to the high end consumer, usually around the business districts and more affluent neighbourhoods in Jakarta. Similarly Australian franchises, Dôme and Gloria Jean’s, have established themselves in the coffee shop market.

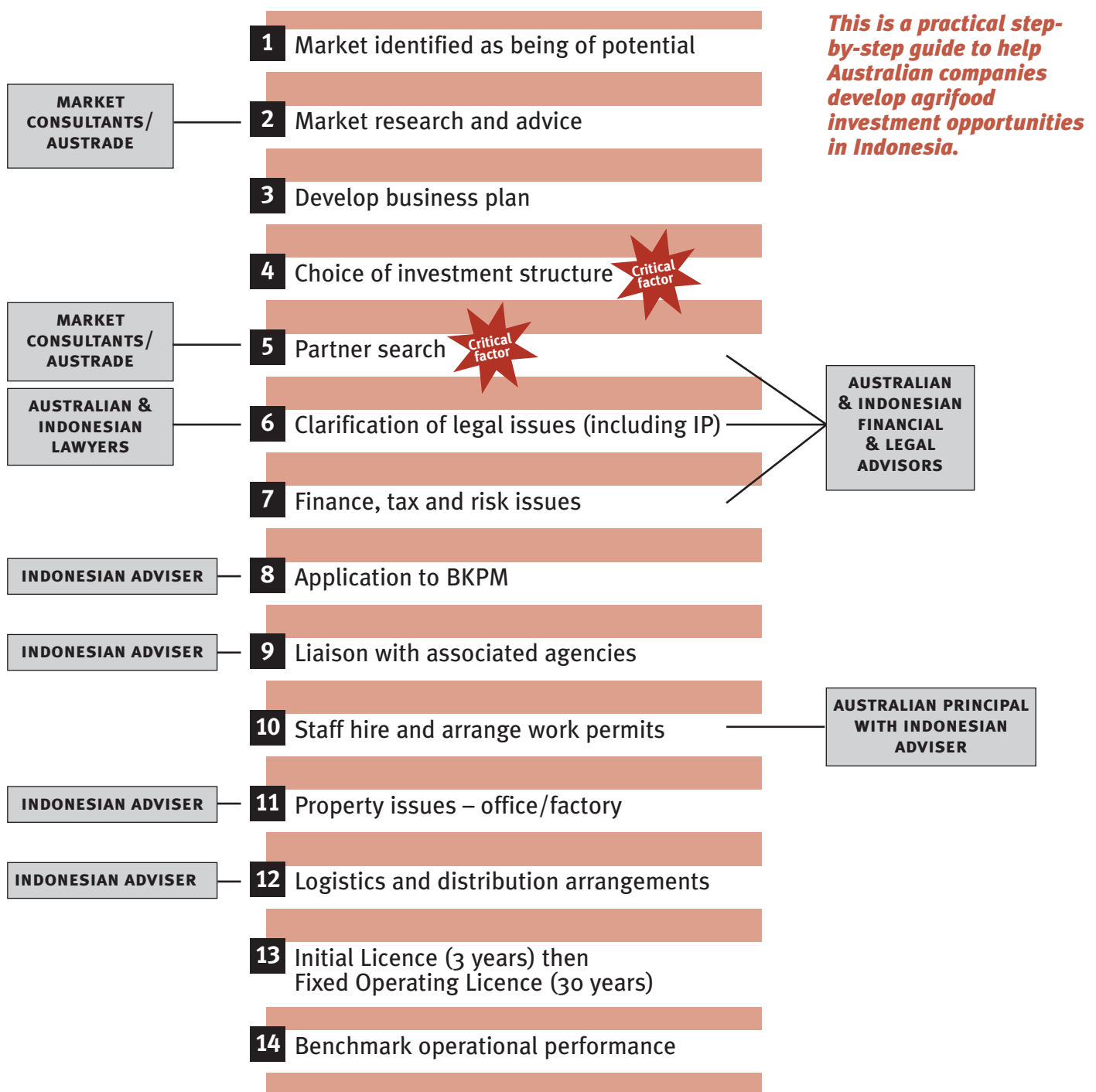
Other recent Australian franchises in Indonesia include La Porchetta from Melbourne.

Regional franchises, notably from Singapore and Malaysia, have captured considerable market share. The high profile Bread Talk franchise from Singapore, offering a range of bread-based snacks in an open kitchen format is a strong attraction in shopping malls.

A significant number of the operators of local franchises come from the younger generations of wealthy Indonesian families. Fast food franchises have a certain cachet among this demographic group as one of the quickest ways to generate cash flow and establish a business presence. As a result there is now an oversupply of ‘me too’ outlets, often trading below expectations.

Any new entrant at this end of the market does need an appealing value statement and image. Products need to be ‘romanced’ to meet youth market tastes and aspirations. Australian companies in this sector are advised to undertake careful market analysis and avoid anecdotal claims of rich rewards.

Figure 4: **STEP-BY-STEP APPROACH TO INVESTMENT**



## PART THREE: AREAS OF INVESTMENT OPPORTUNITY

### CHARACTERISTICS OF THE INDONESIAN FOOD SECTOR

Recent estimates place the total value of the Indonesian food and beverage market at US\$22 billion.<sup>21</sup> Imports account for about 15% of the market. Processed foods production in 2002 was valued at about US\$10 billion.<sup>22</sup> By comparison, the Australian foods and beverage market was estimated at A\$65.9 billion in 2002–03.<sup>23</sup> Indonesia ranks ahead of other Asian countries such as Hong Kong, the Philippines, Thailand, Malaysia and Singapore in total agrifood market size.

- Growth in Indonesia’s total food production has been strong, increasing by 14% between 2000 and 2004.<sup>24</sup>
- Price inflation during the same four year period has been high. Growth in the purchase price index in the ‘modern’ trade sector (supermarkets, hypermarkets, convenience stores) rose 43% in 2004, while the increase for ‘traditional’ outlets (wet market and similar) was 19%, producing an aggregate figure for Indonesia of 25.7% in consumer prices. This is compared with the 2003 figure of 14.1%. Indonesia’s CPI increased by 6.3% in 2004.<sup>25</sup>

A number of trends are evident in the Indonesian food sector, driven by a combination of increased consumer awareness and education, as well as a shift in consumer purchasing power. These have been quantified by the ACNielsen<sup>26</sup> group, which is the principal source of data on consumer expenditure in Indonesia. ACNielsen divides consumer groups into seven income sectors on the basis of monthly household expenditure and they are outlined in Table 4.

Table 4: ACNIELSEN MEDIA RESEARCH DEMOGRAPHIC SEGMENTS

SEGMENT	MONTHLY HOUSEHOLD EXPENDITURE RUPIAH PER MONTH	US DOLLARS PER MONTH*
A1	2,250,000 and over	244 and over
A2	1,750,000 – 2,250,000	190 – 244
B	1,250,000 – 1,750,000	135 – 190
C1	800,000 – 1,250,000	87 – 135
C2	600,000 – 800,000	65 – 87
D	400,000 – 600,000	44 – 65
E	400,000 and below	44 and below

\* EIU average annual exchange rate for 2004 of 1USD = Rp9,222

In 2003, 32% of Indonesian households were in the D and E segments, while in 2004, this figure dropped to 24%, indicating a move of 8% of consumers into the higher expenditure A1 to C2 segments. The urban population continues to dominate consumption trends, with a high concentration around Jakarta.

Consumer sentiment remains high, even in the face of the long-overdue adjustments to heavily subsidised fuel prices that took effect in March 2005.

<sup>21</sup> DFAT, Subsistence to Supermarket II – Agrifood Globalisation and Asia – Vol III.

<sup>22</sup> USDA Foreign Agricultural Service – Indonesia Export Guide 2004.

<sup>23</sup> DAFF, Australian Food Statistics 2004.

<sup>24</sup> FAOStat database (See Appendix D).

<sup>25</sup> EIU – Quarterly Economic Indicators, 22nd March 2005.

<sup>26</sup> <http://www2.acnielsen.com/site/index.shtml>.

Some of the key factors and trends evident in the Indonesian processed food market are as follows:

- The financial crisis of 1997/98 forced Indonesian families to spend considerably less on food items. This has had a severe, ongoing impact on demand for higher value offerings. Retailers' responses have frequently been to increase their range of house brands and lower cost ranges.
- The proportion of house brands will continue to increase, in line with trends in other Asian markets.
- An increased emphasis on health and nutrition is driving food purchasing behaviour. This is not confined to the A and B household segments (as defined in Table 4). Sales of nutritional supplements are growing quickly and the market for functional foods will expand.
- Emphasis on convenience foods will increase, including prepared and easy-to-prepare meals. The growth in instant noodle consumption is a measure of consumer preference for flexible, easy-to-cook meals. Indonesia is a world leader in instant noodle production.
- 'Sachet marketing'<sup>27</sup> will continue to be critical for many multinational food producers, whose distribution networks reach to street corner level. Local producers are, however, increasingly challenging the MNCs in this market sector.
- Baby food and infant formula remain high-growth areas.
- Dairy foods will continue to increase their market share from a small base with milk and cheese being high growth categories.
- Bottled water sales in Indonesia were strong between 2000 and 2003, with growth stabilising at 8% in 2004. Beverage producers are concentrating on energy and health drinks, both of which are also high-growth areas.
- Fast food is now embedded in the Indonesian diet. According to a recent ACNielsen survey, 28% of Indonesians eat 'modern' fast food at least once a week.<sup>28</sup> Lunch is the most popular meal for fast food.
- Products with high sugar content will continue to dominate the confectionery sector, but with an underlying trend to healthier products. Sugar substitutes are an increasingly important factor in food processing.
- Overall the penetration of international consumer trends is now higher than previously observed.

## FRUIT AND VEGETABLES

OPPORTUNITY	MARKET SETTINGS AND TRENDS	COMMENTARY
Tropical fruit production and processing	Consistent supply of raw material often proves a challenge and ventures have failed because of irregular deliveries and variable quality. Opportunities are nevertheless available, notably for export, providing that sound supply relationships can be negotiated with local farming communities.	Pineapple processing has been undertaken and has reasonable prospects. Mangoes represent good potential if supply chain and handling arrangements can be improved.
Vegetable processing	Many ventures are succeeding, but usually on a limited scale. Several potato projects have been undertaken.	Potatoes represent a sound opportunity if associated factors can be resolved. Demand for the end product is good but production, handling and processing issues still need close attention.
Intensive vegetable processing	Good prospects exist for production of french beans, chillies, and other intensive crops which can be grown on small holdings.	Many good operations exist but with limited production capacity. Success is highly dependent on supply agreements with farmer groups.

<sup>27</sup> Sachet marketing is a micro-selling technique aimed particularly at consumers in large, developing economies such as China, India, Indonesia and Brazil. The essence of the strategy is retailing products in micro package sizes, enabling consumers on low incomes to gain access to a product that would otherwise be beyond their price range. This packaging system delivers higher turnover to the manufacturer as well as reasonable profit margins from a much greater number of buyers.

<sup>28</sup> ACNielsen, *Asians the world's greatest fast food fans*, Jakarta, 2005, viewed 18 May 2005, <<http://www.acnielsen.co.id/news.asp?newsID=107>>.

The fruit and vegetable markets of Indonesia are highly dispersed across the archipelago, although Java accounts for some 60% of total Indonesian production. The highland areas in West, Central and East Java are the principal production centres.

Post harvest handling and distribution are areas requiring development. There are few large scale farming ventures in Indonesia – mainly in Java. Land ownership policies and practices are major constraints on high volume production. Several ventures outside of Java, notably in tropical fruit, are attempting larger scale production, but inter-island transport charges are high and inhibit the commercial developments in out-lying islands.

Citrus production has grown strongly, with orange production reaching 1.6 million tonnes in 2004.

The Singapore Government has promoted a project in the Riau Islands for the production of leafy green vegetables for the Singapore market. It is now operating effectively.

Production and distribution constraints continue to inhibit fruit and vegetable projects. But when these issues are resolved, markets both within Indonesia and for export are expected to develop substantially.

## DAIRY PRODUCTS

OPPORTUNITY	MARKET SETTINGS AND TRENDS	COMMENTARY
Cheese-based products	A good market with sound growth prospects and many Indonesian companies are seeking engagement with Australia. Several are already working with Australian principals to produce block cheese.	A limited number of Australian suppliers can readily find good local associates. There are companies interested in JV operations to produce cheese from Australian curd and also import cheese in bulk and pack for the local market.
Liquid yoghurt drinks	Demand is sound at the high end of the market. Expansion of market reach to the medium/low income consumers will unlock enormous opportunity.	Opportunities appear to lie in developing a strong brand in association with an existing Indonesian dairy producer.  The variability of cool chain capability is of particular concern.
Establishing integrated dairy operations	The business climate is improving for commercial investments, and an integrated model appears most appropriate.	PT Greenfield (an Australian start-up company) has demonstrated that investment in this sector is viable, with a strong local partner.
Flavoured milk	Limited market, satisfied by existing dairy companies.	Some potential may exist for licensing brands.
Ice cream and dairy ice confectionery	This is an upper income range market with limited growth potential.	Potential to develop niche products in A1 income group market. <sup>29</sup>

Indonesia's dairy market is growing at 12% per annum (p.a.), with excellent prospects as dairy products increasingly form part of the Indonesian diet. Imports currently account for about 70% of consumption. This proportion will decrease as local ventures expand production.

Indonesia is one of the few dairy markets in the world which is dominated by powdered milk, representing more than 50% of consumption. This is changing as cold chains develop and improve. Most local production from cooperatives is converted to powdered milk. Individual dairy farmers typically own 2–3 cows. Indonesian per capita milk consumption, at 6–7 litres p.a. is low.

Indonesian milk processors are competitive and highly efficient. They include Nestlé (Switzerland), Friesche Vlag (Netherlands), Nutricia (Netherlands), Indomilk (Salim Group) and

<sup>29</sup> A1 is an ACNielsen rating of households expenditure of more than Rp2,250,000 (US\$244) per month (see Table 4).

Ultra Jaya. A more recent entrant is PT Greenfields, a joint venture operation between AustAsia Exports of Australia and the Japfa Group of Indonesia. Greenfields' integrated dairy has 2,500 cows in East Java and produces fresh and long-life milk and other related products.

There is excellent potential for cheese production, which is growing strongly from a small base. Cheese is increasingly finding its way into the Indonesian diet. Infant formula also continues to experience high sales growth.

## BEVERAGES

OPPORTUNITY	MARKET SETTINGS AND TRENDS	COMMENTARY
Introduce new technology for bottled water production	A strong market with sound growth prospects but with high profile MNC competitors. Collaboration with an Indonesian or established South East Asian producer is a possibility.	Demand is likely to outstrip supply as competition for natural spring water exceeds availability and environmental factors impact on spring water sources.
New fruit blends based on strong brand promotion	Demand is growing but the market is highly price-sensitive. The upper end market is quality conscious. There are opportunities for brand development.	This category is expected to undergo fast growth but the challenge will be to tap the middle/low market sectors with competitive offerings.
Health drinks – fortified juices and blends	High end consumers are responsive to functional beverages. Volumes are currently low but growth prospects are promising.	Good local companies would be attracted to producing and supporting a branded product with a track record in Australia or other markets.
Energy drinks	'Red Bull' (premium) and 'Extra Joss' (mass market) have entrenched positions, but this is a fickle market where brands with innovative consumer propositions can capture market share.	These products require considerable promotional support, in media and local point of sale promotion.
Specialty fruit concentrates and premix for 'smoothies'	Some potential at high end of market.	Low volume for premium market.
Sports (isotonic) drinks	A growing market segment where global brands are making inroads.	Potential exists for a locally branded product but brand establishment costs would be high.

The most dramatic influence in the Indonesian beverages market has been the growth of bottled water sales, driven by consumer demand for safe drinking water. The market is dominated by the PT Aqua Group – now owned by Danone of France. Most bottled water sales are in 20 litre packs.

The carbonated drinks sector has been static, largely as a result of luxury taxes. However, these taxes have been removed in January 2005 and greater growth potential can be expected. Soft drinks registered an overall 13% sales growth in 2003, easing to 8% in 2004.

High growth categories include fruit-flavoured drinks. They are targeted across all income groups and are competitively priced.

Energy drinks are a strong performer with brands such as Red Bull and Extra Joss recording more than 15% growth in sales. 'Health' drinks are increasingly popular, offering a range of nutritional benefits.

The Indonesian beverage sector is becoming more highly differentiated, which provides excellent market opportunities for niche brands. These can rapidly establish consumer loyalty, backed by strong local promotion.

## MEAT PRODUCTS

OPPORTUNITY	MARKET SETTINGS AND TRENDS	COMMENTARY
Poultry-based products	Chicken nuggets are a particularly popular item. Other chicken-based products are well-accepted but the limited availability of cold storage capacity hinders volume sales.	There are opportunities to differentiate a new product from standard offerings – either as fast food accompaniments or branded supermarket lines.
Integrated poultry production	The market is dominated by strong producers with extensive supply chain capacity.  Feed milling/supply links are critical.	Possibilities may exist to work with an existing producer for slaughter and production of finished product.
Beef products	Beef remains a premium product but there are possibilities for expanding sales of extended beef-based foods, such as meatballs.	The ‘modern’ beef sector produces quality product for the high end market. New markets for derivative products offer best potential for market entrants.
Feed lotting	A range of companies are strongly embedded in this market, either Australian or Australian-related.	There are significant hurdles to market entry and limited opportunities for new market entrants.
Goat farming	Intensive goat farming appears to have good potential.	Some veterinary issues remain to be resolved concerning Australian breeding goat imports.

Indonesia’s total meat consumption is low – at 10–13 kg per capita p.a. The major meat groups are poultry, beef and goat. Pork is produced in the Riau Islands exclusively for export to Singapore.

Chicken meat is the major category and production has now recovered to pre-1997 levels of 1,100,000 metric ton in 2004.<sup>30</sup> Industry sources forecast poultry consumption to grow at 10% p.a. over the next 3–5 years. Processed chicken products, such as nuggets are very popular. About 80% of poultry sales are sold through wet markets.<sup>31</sup>

Five poultry producers currently account for about 75% of Indonesia’s production, with Thailand’s Charoen Pokhphand group being the market leader.

Indonesian beef consumption is low at 2.4 kg per capita p.a. The industry distributes production from local cattle, including buffalo, as well as beef produced from imported Australian feeder cattle, mostly raised in modern feed lots. Beef is very popular but limited incomes have constrained industry expansion.

The Indonesian beef industry suffered badly between 1997 and 1999, but production has now returned to pre-1997 levels.

Australia supplies most of Indonesia’s requirements for feeder cattle. A number of Australian companies are active in supply and feedlot operations, including AustAsia Exports, CPH and Heytesbury.

<sup>30</sup> FAOStat database, 2004.

<sup>31</sup> Traditional markets that operate with little, if any, modern refrigeration.

## BAKERY PRODUCTS

OPPORTUNITY	MARKET SETTINGS AND TRENDS	COMMENTARY
Bakery ingredients	The market is experiencing solid growth and is well-supplied at both the premium and the price-sensitive end.	Potential exists for working with existing suppliers to produce speciality lines such as fruit and nut-based fillings, flavours and additives.
Bakery operation	This is a crowded market with many competitors.	Profit margins are low except for specialty outlets.
Bread-based franchises	New franchises are doing well, likely to be followed by 'me too' operations.	A high 'fad' component applies to these franchises, but Singapore companies have demonstrated the popularity of innovative bread-based snacks.
Noodles	There are several dominant players with extensive distribution networks.	Existing manufacturers are innovative and new brands are constantly appearing. Pricing is extremely competitive and there is little prospect for new foreign investments.

The Indonesian bakery sector is large and highly fragmented. There are about 10,000 bakeries in Indonesia, ranging from low quality shops to world class establishments.

Flour production is dominated by the Bogasari (Salim) group which operates two of the world's largest flour mills. Australia is a major supplier of wheat to Indonesia, with a market share of around 60%.

Wheat-based products such as instant noodles have strong consumer appeal for convenience factors. Products enjoying high sales growth include instant noodles, breads, cakes, pastries and pizza.

The growth of the Asian instant noodle market represents one of the major shifts in Asian consumption patterns, with Indofood of Jakarta now one of the world's largest producer of packaged noodles.

In the fast food sector, bread-based franchises such as Singapore's Bread Talk have become highly popular in modern shopping malls.

In the fast food sector, pizza outlets are now an established part of the retail scene. Pizza Hut operates more than 100 outlets in 20 Indonesian locations.

Biscuits are a standard item in Indonesia and companies such as Arnott's are providing Indonesian consumers with new lines such as a wafer style version of their iconic Tim-Tams.

## CONFECTIONERY

OPPORTUNITY	MARKET SETTINGS AND TRENDS	COMMENTARY
Chocolate-based products	Many competitors, including MNCs such as Nestlé, Mars, Cadbury-Schweppes and others.	Niche opportunities exist, mainly at the premium end of the market. Co-investing in new brands with an established producer is likely to be the most effective form of market entry.
Sugar-based hard confectionery and gum candies	A very crowded market, well-segmented with both MNCs and local companies.  Access to a strong distribution chain is critical to success.	Licensing and brand development with a local company would be the preferred and safest method of entering the market.
Functional confectionery products – muesli bars, energy bars	A premium product category where MNCs have strong brands (e.g. Milo).	Potential again for licensing with one of the Indonesian producers, but market volume is limited and growth would be off a small base.

The Indonesian confectionery industry is dominated by global brands. A myriad of local producers also occupy market niches, offering specialty lines or servicing regional markets.

Chocolate-based products are popular and companies such as Nestlé and Cadbury-Schweppes are major players in Indonesia. The Mars group also has an operation in Indonesia, offering its global brands. Indonesia is one of the world's leading cocoa producers.

The confectionery sector is mature and experienced only moderate growth of 2.1% between 1998 and 2003.

Fruit gum candies are particularly popular in Indonesia and a profusion of brands compete in this crowded market sector.

The growth of supermarkets and hypermarkets has helped to grow confectionery sales, notably of chocolate-based products.

## SNACK FOODS

OPPORTUNITY	MARKET SETTINGS AND TRENDS	COMMENTARY
Branded snacks such as chips, corn and potato-based	Increasing trend towards potato-based snacks.	There are very high market entry barriers including cost of brand development and distribution.
'Healthy' snack foods and bars	The upper end of the consumer market will increasingly take up these lines, but competition will be intense.	Selective market opportunities could be accessed by working with a supplier at the premium end of the market.
Nut-based products	Very strong local competition and a good raw material base.	Potential could exist for unique or highly tailored formulations in association with an existing manufacturer or well-established distributor.
Novelty items	The Indonesian market will always be attracted to new lines with popular and fashionable themes, often featuring the latest movie, sporting or cartoon heroes.	Probably an area for larger firms with strong promotion and distribution networks, who are receptive to developing new product lines.

Most Indonesian snack foods are traditional items, available at every street corner.

The snack foods market has been valued at US\$450 million, with traditional snacks accounting for 60% of consumption. Peanuts and other nut-based snacks have a high (20%) market share while Western-style snack foods make up the remaining 20%.

Snacks are a major part of the daily diet for Indonesians, with traditional items such as tempeh.<sup>32</sup>

This industry is also highly fragmented, with a high proportion of small and medium-size suppliers.

## BABY FOOD

OPPORTUNITY	MARKET SETTINGS AND TRENDS	COMMENTARY
Traditional baby foods	Dominated by MNCs and huge cost barriers to market entry to replicate product penetration at village level.	Prospects may exist in working with major companies on co-production of specialty formulated lines.
Infant formula	Dominated by MNCs.	House brands may have limited appeal in this sector.
Infant foods	High emphasis on child nutrition is driving strong market growth.	Potential for working with local companies to develop healthy and nutritious brands, particularly drawing on success in Australia or other markets.
Healthy child snacks	Growing demand at the top end of the market may in time lead to broader opportunities in the mass market.	Australian companies with a strong track record will probably attract interest from Indonesian companies seeking proven brands and concepts to develop.

Indonesia is a major market for infant formula and baby foods, and the world's leading MNCs are heavily entrenched. These companies operate extensive marketing programs at village level, often in association with local healthcare organisations.

Intensive consumer education on infant nutrition has resulted in increased consumption of quality infant formula, either as a supplement or as a replacement for breast feeding.

The major suppliers are Numico, Sari Husada (SGM brand), Indofood (Gerber), Heinz and Nestlé.

<sup>32</sup> Tempeh is a fermented soya bean 'cake' and a highly popular item.

## FOOD INGREDIENTS

OPPORTUNITY	MARKET SETTINGS AND TRENDS	COMMENTARY
Ingredient formulation	There are excellent growth prospects, particularly in ingredients for convenience foods and basic processed foods.	Indonesian companies are well-positioned to enter into collaborative business associations in blending and formulation of ingredients.
Seaweed processing	A developing area where global demand is high and Indonesia is a rich source of raw material. Processing close to source makes economic sense.	International agencies such as the International Finance Corporation <sup>33</sup> (IFC) are keen to support the industry.
Fruit-based fillings	Good potential but a highly competitive sector.	Australian products are well-recognised in the market. Greatest potential lies in dried fruits, apple and temperate fruit fillings.

Food processing requires an array of ingredients – from complex flavours, colours and fragrances to common salt, dried fruit and spices.

Indonesia’s food regulatory authority (BPOM) now requires high levels of disclosure for processed food including additives and ingredients.

The food ingredient market in Indonesia is made up from approximately 60% local production and 40% imports, with an increasing move to import replacement for many ‘intermediate’ ingredients. Australian companies Cheetham Salt and KH Foods are now major ingredient producers in Indonesia.

<sup>33</sup> The IFC is a member of the World Bank Group and finances private sector projects in the developing world.

## PART FOUR: TIPS AND RECOMMENDATIONS

- **Study the Indonesian market intensively to decide whether some form of investment is appropriate to build and extend your international markets.**
- **Talk to as many companies as you can in similar sectors and of comparable size. Study ventures that did not work – and find out why. Determining the reasons for failure are as valuable as knowing the ingredients of success.**
- **Government agencies have a vast amount of information and support services available and much of it is free of charge. Appendix D provides further details.**
- **You will need sound advice and professional support to establish an operation in Indonesia. Choose advisers carefully and make sure the fit is right for your business and scale of operation. Talk to Austrade, EFIC and your state government export and investment advisers for further recommendations.**
- **Join networking groups such as the Australia Indonesia Business Council and attend relevant seminars and workshops. Developing an understanding of a range of case studies is particularly valuable for building your own business model.**
- **Before visiting Indonesia, check out Indonesia Australia Business Council events. It is particularly useful to coincide your visit with one of these events, as they can provide access to a wide range of Australian business people based in Indonesia, and an opportunity to learn from their experiences.**
- **Check with Austrade on trade mission visits from Australia to Indonesia as these can provide useful leads and connections. Make sure you build your own visit program around the mission – particularly by remaining after the mission has left to follow up directly on the contacts you have made.**
- **In a similar vein, advise the Australia Indonesia Business Council and the commercial section of the Indonesian Embassy in Canberra or the Indonesian Consulates in the capital cities of your interest in making contact with Indonesians visiting Australia in your area of interest.**
- **Take special care when assessing investment partners and do a lot of desk research, supported by checks with other companies and agencies.**
- **Plan market visits with great care and ensure that your prospects are well-briefed on your company, its activities and your aspirations.**
- **Invite prospective partners to Australia to assess commercial ‘fit’. Check EMDG programs for funding support.**
- **Develop a medium- and long-term perspective on Indonesia which fits your business plan, noting that Indonesia has been subject to a range of political and economic cycles that impact on business.**

Indonesia is a large, diverse and growing agrifood market of considerable investment potential. In recent years, while the country weathered the worst economic shake-out in a generation, much new investment was put on hold.

Today there are signs of sustained recovery and the Indonesian Government is exhibiting new resolve to confront a range of governance issues that have also impeded foreign interest. Investment in Indonesia still requires astute planning and careful implementation. The potential rewards of consolidating a position in one of the largest agrifood markets in the world, and one that also borders Australia, deserves careful consideration by Australian agrifood companies as they look beyond Australia to their regional future.



**Investment Guide  
to the  
INDONESIAN  
Food and Agriculture  
Sector**

**Appendices**

## Appendix A: VIEWS FROM THE AUSTRALIAN BUSINESS COMMUNITY

### **IMA Asia, an associate of the Economist Corporate Network**

*Richard Martin, Managing Director of IMA Asia*, an affiliate of the Economist Conferences Group, observed that, in terms of investment in Asia, Australia's focus is overwhelmingly on China. He suggested that, in general terms, China represents around 70% of Australian companies' current investment interests in Asia, India some 15% – with other Asian markets taking up the rest. Not all that interest of course is expected to translate into actual investment, but China is seen very much as the essential strategic play for most major international companies. Its importance in investment terms dwarfs the rest.

Nevertheless, there are strong indications that Indonesia's economy is improving. Much depends on the new administration of President Susilo Bambang Yudhoyono. Richard Martin summarised, 'Companies can do well in Indonesia, but they require capable managers on the ground, often of the old school, who can manage a low asset business with variable cash flow and have an innate understanding of risk and return.'

### **Views of a leading Australian corporate lawyer**

One of Australia's top corporate lawyers, with many years' experience in Indonesia, remarked that following the financial crisis of 1997/98 up until the election of the government of President Susilo Bambang Yudhoyono, there had been a marked reluctance among major Australian companies to consider investment in Indonesia. He noted that corporate concerns centred around uncertainty in the administration of commercial law, opacity in government decision-making processes, increasing concern at Australian board level with governance issues in Indonesia and apprehension that regional autonomy policies were adding a further layer of cost, regulation and uncertainty to business operations.

'There are a range of positive signs emerging and the business community is waiting for concrete decisions on the legal environment as well as clarity in policy direction. Outstanding legal cases that have clouded perceptions for foreign investors must be resolved quickly, and the government is clearly making a concerted effort to do so.'

'The Australian Government's supportive role is also key to reinvigorating bilateral investment deals. John Howard took a strong stand in supporting the Indonesian Infrastructure Summit in January 2005 and emphasised the importance of new investment in Indonesia. The Australian business community is taking notice. The timing is right for Australian companies to reassess Indonesia's investment potential. The economy is on an up-tick and equity markets in Indonesia are improving.'

### **Major Australian corporate group**

*Washington H. Soul Pattinson and Company Limited (WHSP)*, through its subsidiary, KH Foods Limited (formerly Keith Harris & Co.), has positioned itself strategically in the Indonesian food additives market. WHSP has consolidated its relationship with the flavorings and additives company PT Jutarasa Abadi in Jakarta, to provide an efficient, low cost manufacturing base for the South East Asian region.

Mr Robert Millner, Chairman of WHSP, noted that Indonesia offers considerable potential as a manufacturing base for its Asian operations. Millner emphasised, however, that the key to success in Indonesia is the selection of a suitable local partner. 'The right partner is basic to any long-term strategy,' Millner said. Moreover, by establishing a local low-cost, manufacturing operation in Indonesia, whilst supplying core ingredients from Australia, a company can gain access to food processors servicing that lower cost end of the market.

‘These are often companies unable to afford imported ingredients. Local manufacture can unlock the considerable, untapped demand of efficient, low-cost food processors in the Indonesian market’, Millner said.

Mr Millner also noted that the new government of President Susilo Bambang Yudhoyono was sending the right messages to the international investment community, and that the President knew what was needed for an investment-led recovery. Millner stressed, however, that the foreign investor wanted concrete action to support policy initiatives.

One of Australia’s leading agribusiness investors with a high exposure in Asia also shared his experiences. Some of his key observations were:

‘In 1997/98 nearly everyone got burnt in Indonesia. But it also opened M&A and other opportunities. The Indonesian domestic market is huge, particularly in the major cities, especially Jakarta, where there is an increasingly sophisticated middle class. Distribution capability is always problematic, particularly for fresh, chilled and frozen product.’

‘The Indonesian retail sector is now more sophisticated, but improved retailing skills are not evident outside Jakarta. Food processing companies wanting to buy into the market or operate in Indonesia are finding it difficult to find distributors with good discipline in the cold chain.’

‘If investing in Indonesia – the cheapest thing is labour. But to make food products, labour is rarely more than 10–15% of variable cost. Labour costs in Indonesia are about one sixth of what they are in Australia. But because Indonesians don’t have the same skill level, it is not comparing like with like. Labour savings are also not a direct comparison – as there has been not enough investment in training the Indonesian workforce in quality standards. It is not at all apparent what you need to do to compensate for skills development.’

He concluded:

*‘You need to find solid joint venture partners who have good connections. Connections are always important – but these days’ commercial skills and market savvy rank higher. I need someone who understands the dynamics of my industry and has a vested interest in ensuring a project will work – plus a financial commitment.’*

### **Leading Australian agribusiness investor**

## Appendix B: THE SINGAPORE CONNECTION

Indonesia and Singapore have many longstanding and traditional trading and investment links. These have been further strengthened by Singapore's role as a regional trading centre and its geographic proximity to Indonesia. Singapore's level of engagement has grown considerably in recent years, and Singapore is now one of the largest foreign investors in Indonesia. Agrifood is of special interest, notably estate crops such as cocoa and palm oil.

Singapore's investment role in Indonesia has always been significant in view of the country's highly developed financial sector and its role as a global investment centre. There are also long-standing family linkages between the ethnic Chinese communities of Singapore and Indonesia, with many family companies having major investments in both countries.

A range of Singapore government agencies and government-linked companies are also active in Indonesia, as is the Government of Singapore's investment arm, Temasek Holdings. Singapore's Economic Development Board has provided strong support to projects in Indonesia for the production of leafy green vegetables for the Singapore market as well as pig farming on Pulau Bulan, with the output exported to Singapore.

The Government of Singapore has, through its export promotion arm, *International Enterprise Singapore* established *Network Indonesia* to foster connections and business linkages between companies that have an interest in the Indonesia market. It also aims to cultivate a fraternity of Singapore-based companies and entrepreneurs interested in business opportunities in Indonesia, to share timely information, ideas, opinions and experiences.

Australian companies contemplating investment in Indonesia may find it useful to consider corporate linkages with Singapore-based companies already in Indonesia. Singapore companies with food-related interests are always interested in new technologies for agrifood-processing, which Australia can often provide. Associations with Singapore companies in the food sector can spread risk and also open new lines of finance. The Government of Singapore is strongly backing ventures in Indonesia, and Australian companies who bring technology and practical expertise are generally welcomed in these types of partnerships. Finding the right association naturally takes time and effort, however, there are a number of Australian and Singapore government agencies that can offer advice, as well as many business and financial advisers who can give assistance as well. These include:

- Austrade <http://www.austrade.gov.au>
- The Australia Singapore Chamber of Commerce and Industry <http://www.ascci.org.au>
- Australian Government Department of Foreign Affairs and Trade <http://www.dfat.gov.au>
- International Enterprise Singapore <http://www.iesingapore.com>

Association with a Singapore partner may also provide a broader regional focus and access to other ASEAN markets as well. As Indonesia's economy recovers, the level of Singapore investment in Indonesia is forecast to increase. The two countries recently signed an Investment Protection Agreement – a key element in the bilateral business relationship. Singapore is keen to add value to Indonesian agricultural commodities such as cocoa, and access its strong international trading and transport links to export finished product to overseas markets.

## Appendix C: A SELECTION OF FINANCIAL AND BUSINESS ADVISERS ON INVESTMENT IN INDONESIA

The following are some organisations with experience in Indonesia. There are many groups well-qualified to provide advice on investment in Indonesia. Prospective investors are encouraged to seek advice from a wide range of sources – and evaluate all recommendations most carefully.

### Allens Arthur Robinson

Ezekiel (Zeke) Solomon  
Partner  
Level 17, The Chifley Tower  
2 Chifley Square  
Sydney NSW 2000  
T: +61 (0)2 9230 4380  
E: Zeke.Solomon@aar.com.au  
W: <http://www.aar.com.au>

### Austrade Jakarta

Mr Rod Morehouse  
Senior Trade Commissioner  
Australian Embassy  
Jakarta Indonesia  
T: +62 (0)21 2550 5330  
E: [rod.morehouse@austrade.gov.au](mailto:rod.morehouse@austrade.gov.au)

### Australia Indonesia Business Council

The major organisation in Australia promoting business linkages between Australia and Indonesia. Members enjoy daily news summaries of key events in Indonesia and a strong program of events and networking functions.  
W: <http://www.aibc.com.au>

### Asean Focus Group Pty Ltd

Peter Church and  
Glen Robinson  
Level 37,  
Grosvenor Place  
225 George Street  
Sydney NSW 2000  
T: +61 (0)2 9258 7878  
F: +61 (0)2 9258 7888  
E: [peter.church@aseanfocus.com](mailto:peter.church@aseanfocus.com)  
E: [glen.robinson@aseanfocus.com](mailto:glen.robinson@aseanfocus.com)

### Deacons Lawyers

Ms Kerry Ryan and  
Ms Elizabeth Hallett  
Partners  
1 Alfred Street  
Circular Quay  
Sydney NSW 2000  
T: +61 (0)2 9330 8360  
F: +61 (0)2 9330 8111  
E: [elizabeth.hallett@deacons.com.au](mailto:elizabeth.hallett@deacons.com.au)  
E: [kerry.ryan@deacons.com.au](mailto:kerry.ryan@deacons.com.au)  
W: [www.deacons.com.au](http://www.deacons.com.au)

### IMA-Asia Pty Ltd

Richard Martin  
Managing Director  
Level 37  
225 George Street  
Sydney NSW 2000  
T: +61 (0)2 9252 4336  
F: +61 (0)2 9252 4339  
E: [richard.martin@imaasia.com](mailto:richard.martin@imaasia.com)  
W: [www.imaasia.com](http://www.imaasia.com)

### Indonesia-Australia Business Council (IABC)

IABC is the Indonesia-based counterpart of Australia-Indonesia Business Council. IABC is highly active and organises a powerful series of meetings and functions. Regular business visitors to Indonesia should make contact with IABC in Jakarta or its branches in major regional commercial centres.  
W: <http://www.iabc.or.id>

### KPMG Indonesia affiliate

Sony Harsono  
Harsono Hadibroto Consulting  
Chief Executive Officer  
33rd Floor, Wisma GKBI  
28 Jalan Jenderal Sudirman  
Jakarta 10210 Indonesia  
T: +62 (0)21 570 4888  
F: +62 (0)21 570 5888  
E: [sony.harsono@hhc.co.id](mailto:sony.harsono@hhc.co.id)

### Nevile & Co Commercial Lawyers

Peter Nevile  
Level 11,  
100 Collins Street  
Melbourne VIC 3000  
T: +61 (0)3 9664 4700  
F: +61 (0)3 9654 6784  
E: [peter.nevile@nevile.com.au](mailto:peter.nevile@nevile.com.au)

### PT Kunci Consulting Indonesia

Ken Allan  
Chief Executive  
PO Box 4992, JKTM,  
Jakarta 12049 Indonesia  
T: +62 (0)21 798 9379  
F: +62 (0)21 798 9379  
E: [kallan2@attglobal.com](mailto:kallan2@attglobal.com)  
W: [www.kunciconsulting.com](http://www.kunciconsulting.com)

## Appendix D: USEFUL WEBSITES

### Department of Agriculture, Fisheries and Forestry (DAFF)

Primary entry point for data on the activities of the Department, including access to a wide range of published material on Australian agriculture, food and international market developments.

<http://www.daff.gov.au>

### Ministry of Agriculture, Indonesia

Website for Indonesia's Ministry of Agriculture with extensive data on Indonesian agriculture and good links to other sites.

<http://www.deptan.go.id>

### Department of Foreign Affairs and Trade (DFAT)

Good coverage of country developments and market access issues.

<http://www.dfat.gov.au>

### Austrade

Austrade services are outlined along with market profiles for food and agribusiness for Indonesia and valuable advice on market entry.

<http://www.austrade.gov.au>

### Investment Co-ordinating Agency (BKPM)

The primary site for Indonesia's investment promotion agency. Includes regulations, procedures and a host of useful information on investment in Indonesia.

<http://www.bkpm.go.id>

### Indonesian Bureau of Statistics (BPS)

The Indonesian government's statistical agency. Its 'Susenas' (Survey Sosial and Ekonomik Nasional) is a source of primary data on Indonesian household consumption and expenditure.

<http://www.bps.go.id>

### Google.com News Alerts.

Useful for establishing news alerts on matters of interest – e.g. listing 'Indonesian investment' in the New Alert Google site will provide daily emails with links back to articles from the international press dealing with Indonesian investment developments – and thus enable the reader to keep up to date.

<http://news.google.com.au>

### The National Agency for Food and Drug Control (BPOM)

Indonesia's regulatory agency for food safety and regulations.

<http://www.pom.go.id>

### Australian Indonesia Business Council

<http://www.aibc.com.au/>

### ACNielsen

The primary source of consumer market research data on Indonesia.

<http://www.acnielsen.co.id>

### International Monetary Fund

Valuable data on Indonesia's economy with sectoral data.

<http://www.imf.org>

### Indonesian Chamber of Commerce (KADIN)

KADIN is the peak business association in Indonesia and has a strong input to government policy.

<http://www.kadin.or.id>

### Indonesian Food and Beverages Association (GAPMMI)

The peak Indonesian industry organisation for the food and beverage industries.

[gapmmi@indosat.net.id](mailto:gapmmi@indosat.net.id)

### International Finance Corporation

The commercial lending arm of the World Bank. Includes very useful data on Indonesia, including several industry reports on agriculture.

<http://www.ifc.org>

### Australian Bureau for Agricultural and Resource Economics

ABARE is an Australian government economic research agency noted for its independent research and analysis.

<http://www.abareconomics.com>

### Sejarah Indonesia

News and views on events in Indonesia.

<http://www.gimonca.com>

### FAOStat Database

The database of agricultural statistics of the Food and Agriculture Organisation of the United Nations.

<http://faostat.fao.org>

## Appendix E: GLOSSARY OF TERMS, DEFINITIONS AND ABBREVIATIONS

ACNielsen	AC Nielsen is one of the world's leading market information companies. It has a base of operations in Indonesia, undertaking a range of functions including retail consumer research, customised research, modelling and analysis of available data.
agrifood	This Guide utilises the definition employed by the Australian Government Department of Foreign Affairs and Trade (DFAT) in their series of publications, Subsistence to Supermarket II. It refers to any food or beverage, or food or beverage material, from unprocessed through highly processed food and beverages.
agrifood-related company	The definition covers all companies involved at any stage in the production, processing, distribution and/or sale of agrifood, whether by the provision of goods and/or services.
AIBC	Australia Indonesia Business Council
Austrade	Australian Trade Commission
BKPM	Indonesia's Investment Coordinating Board
B POM	Indonesia's Food Regulatory Authority
BPS	Badan Pusat Statistik – Statistics Office of Indonesia
CPI	Consumer Price Index
DAFF	Australian Government Department of Agriculture, Fisheries and Forestry
DFAT	Australian Government Department of Foreign Affairs and Trade
EFIC	Export Finance and Insurance Corporation
EMDG	Export Market Development Grants administered by Austrade
FAOStat	The database of agricultural statistics of the Food and Agriculture Organisation of the United Nations
FDI	Foreign direct investment
GDP	Gross Domestic Product
IABC	Indonesia Australia Business Council
IFC	The International Finance Corporation headquartered in Washington DC
IP	Intellectual property
Krismon	The Indonesian term for the financial crisis that was experienced in Indonesia in 1997/1998.
MNC	Multi-national corporation
SBY	The Indonesian shorthand terminology for President Susilo Bambang Yudhoyono
SME	Small and medium size enterprise
WGAFIC	Working Group on Agriculture and Food Cooperation comprising representatives of the Australian Department of Agriculture, Fisheries and Forestry and the Indonesian Ministry of Agriculture.

