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Revitalizing Batam and Bintan Special Economic Zones (SEZs): the Test-Beds for Indonesia's Growth Ambitions

Executive Summary


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Indonesia's ambition to achieve 8% economic growth hinges on improving its investment climate, particularly through enhancing the competitiveness of special economic zones (SEZs) like Batam and Bintan. Inspired by the successful transformation of Shenzhen, China's first SEZ, these regions could serve as pilot zones for transformative economic reforms. However, challenges such as fragmented strategies, dual authority in Batam, ineffective legal frameworks, outdated arbitration laws, and unclear land regulations have hindered FDI. For instance, the missed opportunity of a USD 2 billion data center project that went to Johor, Malaysia. To enhance their appeal as SEZs and drive national economic growth, Batam and Bintan must focus on refining their development objectives, aligning legal standards with global norms, streamlining governance, strengthening infrastructure, and fostering regional collaboration. This policy brief attempts to lay the groundwork for transforming Batam and Bintan into competitive SEZs that can drive Indonesia's economic future.

Identifying the core economic challenges

Indonesia's ambition to achieve 8% economic growth relies on boosting investment, with foreign direct investment (FDI) playing a crucial role. However, the current investment climate presents significant barriers. In the 2024 Index of Economic Freedom by The Heritage Foundation, Indonesia ranks 53rd, with its rule of law—covering property rights, government integrity, and judicial effectiveness—remaining below global averages, deterring potential investors.[1]

Achieving the 8% growth target requires adopting strategies like those transforming Shenzhen, China. Shenzhen's success was fueled by legal autonomy and focused reforms that enabled rapid industrial growth. A similar approach could enhance Indonesia's rule of law and regulatory framework, strengthening its economic governance and aligning with its growth objectives.

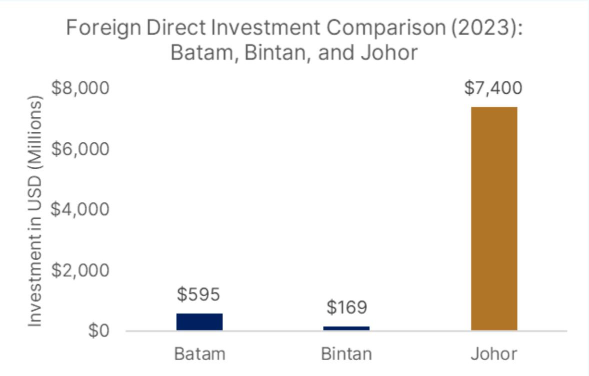
Drawing insights from Shenzhen's SEZ success

In 1980, Shenzhen became China's first SEZ under the leadership of Deng Xiaoping. Its population has since grown from 300,000 to over 17 million today, driven by foreign investment and booming exports.[2] Home to over 14,000 high-tech companies like Huawei, Tencent, and DJI, Shenzhen's GDP now exceeds USD 489 billion—more than double Jakarta's—solidifying its role as a global manufacturing hub and "China's Silicon Valley."[3,4]

Shenzhen's success was fueled by legal autonomy, enabling groundbreaking reforms across sectors. Key strategies include land reforms that commercialized residential land, price-system reforms to ease restrictions on capital goods, and financial reforms allowing foreign banks and financial institutions to enter Shenzhen. Additionally, simplified administrative approval procedures attracted investments by reducing bureaucratic delays. Shenzhen's success highlights the importance of legal and regulatory autonomy for SEZs to attract investments and accelerate growth.

Despite their strategic location along the Malacca Strait, through which 30% of global trade flows, Batam and Bintan have yet to realize their potential as Special Economic Zones (SEZs).[5] They continue to underperform in attracting FDI compared to neighboring regions like Johor, Malaysia, and Singapore, which dominate investment inflows. For instance, Batam and Bintan recently lost a USD 2 billion data center project to Johor, highlighting their competitive shortcomings.[6]

Strategic reforms are urgently needed to elevate Batam and Bintan's competitiveness. As Singapore nears its investment capacity, these regions have failed to capture FDI spillover, underscoring the need to reposition Batam and Bintan as attractive FDI hubs within the regional landscape.



Johor led in FDI in 2023 with $7.4 billion, followed by Batam ($595 million), and Bintan ($169 million). This disparity indicates the pressing need for strategic reforms for Batam and Bintan to enhance their competitiveness in attracting FDI.

Navigating obstacles and barriers

Batam and Bintan are currently challenged by a lack of clear objectives and strategic direction, which risks leading to a "paradox of plenty." This term refers to a situation where abundant resources or potential fail to deliver results due to mismanagement or lack of a cohesive focus. Without a clearly articulated framework for sustainable long-term development, Batam and Bintan may struggle to establish a distinct path toward specialization, placing them at a disadvantage compared to their regional counterparts.

The enactment of the Omnibus Law strives to streamline regulations and simplify licensing processes across regions in Indonesia. As a result, Batam and Bintan must cultivate distinctive economic and investment attraction features to maintain their competitive edge. To become pilot zones like Shenzhen, Batam and Bintan must offer more than the Omnibus Law provides. Competing on the same level won't suffice; they need reforms that extend beyond the law's scope, offering clearer and stronger advantages to fully capitalize on their strategic location, infrastructure, and SEZ status. Without such reforms, they risk losing visibility and competitiveness to potential investors.

The partial application of SEZ's status in Batam has led to significant confusion, primarily due to overlapping regulations that lack coherence. This "patchy approach" stems from the dual authority structure, where SEZ zones fall under separate regulatory frameworks while other areas remain under provincial jurisdiction. This fragmented governance system creates regulatory inconsistency, making it difficult for investors to navigate the investment landscape and diminishing Batam's appeal as a business destination. Furthermore, while economic and market considerations are crucial for fostering growth, political interests exceedingly influence some policies, limiting both regions' potential to serve as engines of industrial growth.

Ineffective rule of law and outdated arbitration frameworks also significantly undermine the investment potential of Batam and Bintan. Batam and Bintan continue to face challenges like inconsistent contract enforcement, cumbersome licensing processes, and bureaucratic delays, all of which deter investors and hinder industrial growth.

Indonesia's Arbitration Law has remained unchanged for 25 years, leaving it outdated and unable to address the complexities of modern dispute resolution. This stagnation has created substantial concerns, such as the lack of regulation for emerging issues and substances that were not previously considered. As a result, investors face legal uncertainty and weakened trust in the business environment.

Along with that, Indonesia only has a Supreme Court regulation on mediation, which holds a lower position in the legal hierarchy compared to formal legislation, thereby limiting its effectiveness. In contrast, Singapore has proactively ratified and implemented the "Convention on Mediation," strengthening its legal framework for dispute resolution and positioning itself as a preferred hub for international arbitration and mediation. This disparity highlights the urgent need for Indonesia to revamp its arbitration laws to remain competitive in the global legal landscape.

Although Batam and Bintan possess competitive physical infrastructure, poor service quality, and persistent regulatory bottlenecks severely restrict their ability to attract and sustain significant investment. These regions urgently need swift change to overcome these barriers and realize their full potential as investment hubs.

Strategic considerations for policymakers

To position Batam and Bintan as pilot SEZs that can attract substantial investment and trigger competitiveness improvements across other regions, several key considerations require deeper exploration:

1. **Leveraging Competitive Strengths: Batam and Bintan should be developed as pilot zones for transformative reforms, aligning with Indonesia's nation-building goals.** These regions can drive sustained growth and competitiveness, serving as models for national reforms that can permeate across the country.

   The development strategy for Batam and Bintan must take a comprehensive approach that includes both short-term and long-term initiatives. In the short term, efforts should focus on immediate regulatory innovations, targeted incentives, and rapid sector-specific investments to stimulate quick growth. Meanwhile, the long-term strategy must emphasize sustainable development through continuous investment in infrastructure, human capital, and strategic planning to ensure these regions evolve into lasting drivers of economic activity.

   On top of that, to avoid the "Paradox of Plenty," a clear, unified narrative is essential domestically and internationally. This narrative should highlight their competitive strengths in sectors such as digital industries, renewable energy, and export-oriented manufacturing. It must remain consistent and enforced across leadership and administrations.

2. **Granting Legal Autonomy (Lex Specialis): To differentiate Batam and Bintan from other regions benefiting from the Omnibus Law, granting them legal autonomy (Lex Specialis) in taxation, labor regulations, and contract enforcement is essential.** While the Omnibus Law has improved the general framework, these regions must offer more—such as higher legal standards, unique incentives, and targeted specialization—to stand out. Like Shenzhen, Batam and Bintan can leverage this autonomy to attract more FDI, drive industrial growth, and become key hubs in Indonesia's long-term economic vision.

3. **Addressing Governance and Regulatory Challenges: A strategy to resolve the dual authority structure in Batam is needed, which has long confused investors.** This reform should aim to reduce political interference and ensure that Batam and Bintan are managed efficiently, similar to Singapore's Jurong Town Corporation (JTC). Furthermore, policymakers should assess the potential of integrating the entire BBK (Batam, Bintan, and Karimun) into a unified Free Trade Zone (FTZ) or SEZ to create a seamless regulatory environment and eliminate the enclave-specific barriers that deter investors.

4. **Revamping Indonesia's Arbitration and Legal Framework:** To strengthen investor confidence, Indonesia must revamp its outdated Arbitration Law (UU No. 30/1999) to align with global standards. This reform requires four critical steps. **a) Arbitration laws should be harmonized with international conventions,** such as the Singapore Convention on Mediation, to ensure consistency and global recognition. **b) Institutional capacity for arbitration and dispute resolution must be improved** to meet international benchmarks. This includes enhancing the training and resources available to arbitration bodies. **c) Specialized arbitration centers should be developed,** positioning Batam as a hub for international arbitration, similar to Singapore's Maxwell Chambers. This would elevate Batam's role in global dispute resolution. **d) Strengthen enforcement mechanisms** to ensure that arbitration decisions are respected and implemented without bureaucratic delays or enforcement challenges, including judicial interference.

5. **Clarifying Land Regulations and Transparency: To create a more favorable investment climate, clear and comprehensive land regulations must be established in Batam and Bintan.** This includes specifying land use categories, terms of lease, and ownership rights for foreign investors. Furthermore, providing public access to detailed land information—such as land availability, zoning regulations, and environmental considerations—will enable investors to make informed decisions more quickly. This improved transparency would not only reduce delays in land acquisition but also build investor confidence by ensuring clarity and consistency in the legal processes governing land usage in these regions.

6. **Strengthening Digital and Logistics Infrastructure:** Batam has immense potential to become a digital and logistics hub, especially with opportunities to house data centers and serve as a transhipment point due to its proximity to major trade routes. Expanding port facilities and developing state-of-the-art digital infrastructure will enable Batam to attract investments. However, such investments must be strategically integrated into Indonesia's long-term national growth agenda to ensure sustained impact.

7. **Enhancing One-Stop Services (OSS): In alignment with Indonesia's commitment to digitalization, the OSS system must be consistently and thoroughly implemented on a digital platform across all government levels to eliminate manual interventions and ensure enhanced efficiency and transparency.** By integrating key business operations—including tax administration, labor permits, land acquisition, utility connections, and regulatory compliance—into a unified digital platform that reaches multiple agencies and regional government levels, Batam and Bintan can streamline the entire business lifecycle, from initial setup to ongoing operational support. Inspired by Singapore's successful OSS model, this will create a more attractive investment climate for both domestic and international investors.

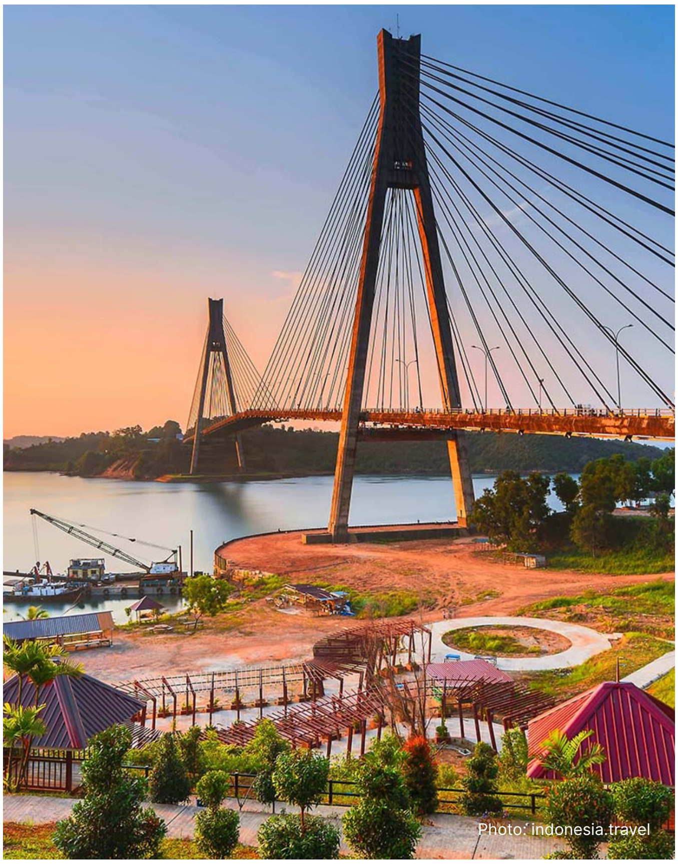
8. **Fostering Regional Collaboration and Strengthening the Growth Triangle: Indonesia must leverage its role as a key player in regional growth triangles, such as the Indonesia-Malaysia-Singapore Growth Triangle (IMS-GT).** By positioning Batam and Bintan as central players in this collaboration, Indonesia can tap into spillover investments from Singapore, especially in sectors like digital services, logistics, and renewable energy. Strengthening regional collaboration and focusing on fulfilling Singapore's supply chain needs (including food, energy, and raw materials) will enhance Batam and Bintan's competitiveness in the regional market.

Charting the future path for Batam and Bintan SEZs

Based on the discussion above, the following questions remain:

Are the proposed considerations enough to ensure Batam and Bintan emerge as impactful SEZs? What additional factors should be considered to secure their long-term competitiveness and success?

This policy brief lays the groundwork for rethinking Batam and Bintan's development, encouraging stakeholders to engage in deeper discussions on the necessary reforms to transform these regions into thriving SEZs that drive Indonesia's economic growth.



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This policy brief is informed by the Focus Group Discussion (FGD) titled **"Strategy for Effectively Establishing Special Economic Zones"** held on October 1, 2024, organized by the Indonesian Business Council (IBC). The FGD featured prominent experts and figures, including **H.E. Suryopratomo** (Ambassador of Indonesia to Singapore), **Dr. Marty Natalegawa, Ph.D**. (Former Minister of Foreign Affairs of Indonesia), **Eri Hertiawan, S.H., LL.M.** (International Arbiter in Singapore and Dubai), and **Prof. Hikmahanto Juwana, S.H., LL.M., Ph.D.** (Professor of International Law at Universitas Indonesia). Their insights and expertise form the foundation of this brief.

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