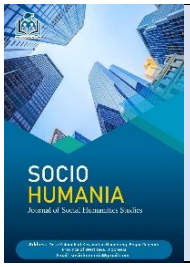

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Reciprocal Tariffs and the Fragility of Global Trade: Economic Impacts on Indonesia's Palm Oil Sector

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ABSTRACT

The implementation of a 32% reciprocal import tariff by the United States in April 2025, targeting Indonesian palm oil, reflects an intensifying global trend of trade protectionism. As one of Indonesia's top export commodities, palm oil was severely affected by the policy, revealing the structural fragility of the country's export-dependent economy. The tariff led to immediate disruptions in trade flows, price competitiveness, and employment across the palm oil supply chain. This study aims to analyze the economic impact of the U.S. tariff policy on Indonesia's palm oil industry and to examine the government's policy responses in mitigating these effects. The research also seeks to identify strategic lessons for improving trade resilience in the face of unilateral trade measures. The study adopts a qualitative descriptive approach, integrating macroeconomic analysis and international trade theory. It uses secondary data from trade statistics, government reports, and international institutions, combined with conceptual frameworks including global value chain theory, comparative advantage, and trade policy response models. The findings indicate that the tariff caused a 22.5% decline in export value and a 24.9% drop in volume within the first quarter after implementation. Approximately 17,000 workers were affected, and investor confidence weakened due to disruptions in downstream value chains. In response, the Indonesian government launched a five-pillar strategy covering trade diplomacy, market diversification, regulatory reform, fiscal support, and digital service trade bargaining. These findings highlight the urgent need for structural transformation, value-added industrial development, and adaptive trade governance to strengthen Indonesia's long-term economic resilience.

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INTRODUCTION

The resurgence of global protectionism, fueled by geopolitical tensions and unilateral trade measures, has challenged the principles of open markets and equitable trade. Among these developments, the United States' imposition of a 32% reciprocal import tariff on Indonesian palm oil in April 2025 marks a significant escalation in trade barriers targeting surplus-exporting countries. Indonesia, with a trade surplus of USD 19.3 billion against the U.S. in 2024, was directly affected, particularly in its palm oil exports—a cornerstone commodity for national employment, rural development, and foreign exchange earnings (**GAPKI, 2024; Shamdasani, 2025**).

Theoretically, this situation underscores key dynamics in international trade. According to the classical theory of comparative advantage (Ricardo, as cited in Krugman, **Obstfeld, & Melitz, 2018**), Indonesia's natural endowments and cost efficiency grant it a strong position in palm oil production. However, external interventions such as tariffs can distort market mechanisms, reduce demand, and cause welfare losses (**Salvatore, 2020**).

Furthermore, the palm oil industry is embedded in global value chains (GVCs), particularly through downstream products like oleochemicals and biofuels (**Gereffi & Fernandez-Stark, 2016**). Disruptions at any point in this chain—such as increased U.S. tariffs—can create ripple effects on employment, investment, and long-term competitiveness. The case also highlights vulnerabilities posed by export dependence, wherein Indonesia's reliance on traditional markets like the U.S. and EU makes it particularly susceptible to policy shocks (**Todaro & Smith, 2020**).

In response, emerging economies often employ adaptive strategies ranging from trade diplomacy and market diversification to domestic policy reforms and regulatory relaxation (**Hoekman & Kostecki, 2009**). Indonesia has pursued similar pathways through the Trade and Investment Framework Agreement (TIFA), export incentives, and structural reforms aimed at mitigating the adverse effects of the tariff hike. This background provides the conceptual and empirical foundation for analyzing the U.S. tariff's implications for Indonesia's palm oil industry—offering insights into the broader tensions between trade liberalization and national economic security.

RESEARCH METHOD

This study adopts a descriptive-qualitative research design, integrating macroeconomic and international trade perspectives to explore the economic impact of the United States' reciprocal tariff policy on Indonesia's palm oil sector. Rather than employing an experimental method, the research relies on policy-oriented analysis supported by secondary data sources. This approach enables a contextualized understanding of trade disruptions, government responses, and sectoral implications arising from tariff imposition (**Salvatore, 2020; Krugman, Obstfeld, & Melitz, 2018**).

The study utilizes secondary data compiled from a range of authoritative sources, including: (1) Trade statistics from the International Trade Centre (2025), Indonesia's Central Bureau of Statistics (**BPS, 2025**), the Ministry of Trade (Kementerian Perdagangan RI, 2025a); (2) Government policy documents, such as reports from the White House and the Coordinating Ministry for Economic Affairs of Indonesia; (3) International reports from organizations like the World Bank (2025) and the World Trade Organization (2025); and (4)

Academic literature to support the theoretical foundation and comparative analysis (**Hoekman & Kostecki, 2009; Gereffi & Fernandez-Stark, 2016**).

Three main analytical frameworks were employed: (1) Descriptive-Comparative Analysis, this analysis compares the tariff structures before and after the implementation of the U.S. reciprocal tariff, including benchmarking against Malaysia, a competitor not subject to the same trade barrier; (2) Sectoral Economic Impact Analysis, the analysis focuses on quantifying the impact on export volume, price competitiveness, and supply chain efficiency, and estimates the implications for employment. Conceptually, a partial equilibrium trade model is referenced to frame the shifts in producer surplus, consumer welfare, and trade flows (**Salvatore, 2020**); and (3) Policy Response Analysis, government policy responses were examined through the review of official statements and trade diplomacy efforts, particularly through the Trade and Investment Framework Agreement (TIFA). Comparative insights were also drawn from Malaysia's experience as a reference point (**SAIAC, 2025**).

The scope is delineated by: (a) Time frame: 2023 (pre-tariff) to early 2025 (post-tariff implementation); (b) Product category: Palm oil and its derivatives (HS code 1511); and (c) Market focus: The United States, as the target of the reciprocal trade policy.

RESULT AND DISCUSSION

The U.S. Tariff Policy and Indonesia's Trade Position

On April 2, 2025, the administration of President Donald Trump enacted a reciprocal import tariff policy under the authority of the International Emergency Economic Powers Act (IEEPA) and the National Emergencies Act (NEA). The policy aimed to penalize countries with significant bilateral trade surpluses against the United States by imposing uniform tariffs on a range of imported goods. By framing trade imbalances as threats to national economic security, the U.S. adopted a protectionist stance that departed from multilateral trade norms governed by the World Trade Organization.

Indonesia was among the countries most affected by this policy due to its substantial trade surplus with the U.S., amounting to approximately USD 19.3 billion in 2024 (**BPS, 2025a**). The imposition of a 32% tariff on several key export products, notably palm oil (HS 1511), represented a significant escalation from the previously applied import duties of between 0% and 5%. In contrast, competing exporters such as Malaysia were not subjected to the reciprocal tariff, as they maintained a trade deficit with the U.S. and continued to enjoy the Most Favoured Nation (MFN) rate of 5%. This discrepancy in treatment reshaped the competitive landscape of the U.S. palm oil market in favor of Malaysia and other non-targeted producers.

The consequences of this tariff policy were immediate and pronounced. The sharp increase in import duties rendered Indonesian palm oil significantly more expensive for U.S. importers, resulting in a notable decline in both price competitiveness and market share. Export data from early 2025 revealed a drop of over 20% in palm oil shipments to the U.S. compared to the previous year (**BPS, 2025b**). Analysts noted that American buyers began shifting procurement to alternative suppliers, including Malaysia, Colombia, and several West African nations, where comparable products were subject to far lower duties.

Beyond palm oil, the policy also affected other Indonesian export categories such as footwear, textiles, and electronic components, all of which became subject to the same elevated tariff rate. Indonesia was considered one of the hardest-hit economies in Southeast Asia due

to its high exposure to the U.S. market and relatively narrow export base. The uniform nature of the tariff disregarded industry-specific conditions and introduced systemic distortions across multiple export-dependent sectors.

In response to growing pressure from producers and industry associations, the Indonesian government initiated a series of policy adjustments. Palm oil producer groups, including GAPKI and the Farmers Union SPKS, lobbied for the reduction or suspension of domestic export levies and taxes in order to absorb part of the tariff burden. At the time, Indonesia applied a progressive export tax on crude palm oil (CPO) of up to USD 196 per ton, a cost that severely limited price flexibility in light of the new U.S. tariff regime. These associations argued that temporarily lifting or reducing the levy could help stabilize export volumes. Policy responses included a downward revision of Indonesia's CPO reference price and adjustments to the sliding scale levy structure. Additionally, the Ministry of Finance introduced administrative measures to accelerate VAT refunds for exporters and provided liquidity support to affected firms.

The economic repercussions extended into the macroeconomic domain. Analysts from DBS and Mandiri Sekuritas estimated that the tariff impact could reduce Indonesia's GDP growth by up to 0.5 percentage points in 2025, owing to the contraction in export earnings and reduced foreign exchange inflows. The sentiment in capital markets also reflected heightened uncertainty, with the rupiah experiencing a brief depreciation toward IDR 17,000 per USD.

At the firm level, many palm oil exporters accelerated their market diversification strategies in response to the U.S. trade barrier. Export destinations such as India, Egypt, Bangladesh, and the European Union became focal points of redirected trade flows. The government's active participation in regional trade agreements like the Regional Comprehensive Economic Partnership (RCEP) and ongoing negotiations for comprehensive economic partnership agreements (CEPAs) with Canada and Peru were part of a long-term effort to reduce overdependence on any single market.

Despite the gravity of the disruption, the U.S. provided a 90-day administrative grace period before full enforcement of the tariffs, intended to allow room for trade consultations. During this window, Indonesia intensified diplomatic efforts under the Trade and Investment Framework Agreement (TIFA), while also using the opportunity to reassess domestic trade facilitation regulations. GAPKI and other stakeholders advocated for broader reforms, including the simplification of non-tariff measures to improve the resilience of Indonesia's trade structure.

This episode serves as a potent reminder of the vulnerabilities inherent in Indonesia's trade architecture. With a heavy reliance on a few key commodities and markets, the economy remains susceptible to exogenous shocks driven by unilateral foreign policy decisions. The reciprocal tariff policy not only exposed these weaknesses but also emphasized the importance of diversification, domestic value addition, and sustainable trade governance. In the evolving global economic landscape marked by protectionism and strategic decoupling, Indonesia must continue to invest in institutional reforms and supply chain upgrading to safeguard its trade interests in the long run.

Economic Impact on the Palm Oil Industry

The imposition of a 32 % U.S. reciprocal import tariff on Indonesian palm oil in April 2025 significantly disrupted the industry's export performance. Data from the first quarter of 2025 indicate a striking 22.5 % decline in export value, dropping from USD 498 million in 2024 to

USD 386 million, accompanied by a 24.9 % reduction in volume—underscoring direct impacts on revenue and trade flows (**BPS, 2025b; Kementerian Perdagangan RI, 2025b**). This abrupt contraction reflected a broader trend of tariff-driven market shock that eroded both competitive positioning and financial returns for producers. The escalation in import duties compelled Indonesian exporters to partially absorb the cost burden, further squeezing profit margins. This strategy was viewed as necessary to avoid complete loss of market share in the U.S., yet it came at the price of eroded corporate financial health.

Such tariff-induced cost escalation reverberated throughout the palm oil global value chain (GVC), particularly affecting downstream industries like oleochemicals and biofuels with established long-term supply agreements in the U.S. The increased input costs and sudden contract disruptions disrupted supply consistency and eroded investor trust (**Gereffi & Fernandez-Stark, 2016**). This signaled a broader structural risk in reliant production networks, leading some investors to pause planned capital expansion in Indonesia.

The economic ramifications also extended significantly into the labor sector. GAPKI (2025) estimated that approximately 17,000 workers across plantations, logistics, and processing facilities were impacted by the tariff measures. This aligns with classical tariff theories, which suggest that protectionist actions can precipitate welfare losses and inefficient resource allocation (**Salvatore, 2020**). These displaced workers faced income uncertainty, particularly among rural labor segments heavily reliant on export-linked employment.

In light of burgeoning pressures, producer associations such as GAPKI and farmer groups like SPKS advocated for temporary policy relief to buffer the sector. Following media reports and public advocacy, the government initiated a series of adjustments: reducing export levies, temporarily waiving export taxes, and expediting VAT and duty refunds for exporters. Such measures aimed to partially offset export cost surges and restore market competitiveness amid trade turmoil.

Despite remedial policy efforts, the industry continued to grapple with volatility. Bloomberg analysis highlighted that the tariff-induced uncertainty suppressed pricing power, undermining Indonesia's ability to compete against regional rivals like Malaysia, which maintained lower export costs and benefited from more favorable duty structures. This scenario underscored the strategic imperative for Indonesia to lower structural transaction costs while enhancing supply efficiencies.

Strategic reactions at both firm and national levels included aggressive market diversification initiatives. Exporters pivoted toward emerging markets in Africa, the Middle East, and South Asia, leveraging trade agreements under RCEP and ongoing negotiations with Canada and European partners. These efforts aimed to reduce over-dependence on the U.S. market and reestablish growth pathways through alternative trade channels. In parallel, public and private sectors jointly advanced investments in value-added capacity and sustainability credentials, such as ISPO and RSPO certifications, to enhance access to premium markets. Analyst commentary pointed to Indonesia's intensified push toward oleochemicals, biofuels, and certified sustainable palm oil as mechanisms to buffer against external shocks and capture long-term demand growth.

Still, longer-term challenges loom. Rising production costs—stemming from increased input prices, aging plantations, and tighter environmental regulations—further compresses profit margins. As domestic production becomes more expensive, the tariff measures threaten to deepen industry vulnerability unless matched by comprehensive structural reform. The U.S. tariff measures generated immediate financial impacts and systemic risks across Indonesia's palm oil industry—from revenue compression and supply disruption to

workforce dislocation. Short-term policy relief provided temporary stability, while diversification and upgrade strategies established a foundation for long-term resilience. Moving forward, mitigating external shocks will require continued cost containment, enhanced value-chain integration, and multi-market expansion to sustain competitive positioning in an increasingly fragmented global trade environment.

Policy Responses and Strategic Mitigation

In the wake of the reciprocal tariff policy imposed by the United States in April 2025, the Indonesian government initiated a multi-faceted response aimed at mitigating both the immediate trade shock and the long-term structural vulnerabilities of its export economy. Recognizing the significant exposure of Indonesia's palm oil sector to U.S. market fluctuations, policymakers quickly mobilized a comprehensive five-pillar strategy. This policy framework addressed diplomacy, market diversification, regulatory reform, fiscal support, and trade asymmetry bargaining, with the goal of safeguarding industry continuity while repositioning Indonesia's global trade standing.

The first pillar focused on trade diplomacy and bilateral negotiations, particularly through reactivation of the Trade and Investment Framework Agreement (TIFA) between Indonesia and the United States. Indonesian trade officials, alongside legal and economic advisors, sought to create dialogue mechanisms for tariff suspension or moderation, while also exploring procedural appeals through regional forums such as the Indo-Pacific Economic Framework (IPEF) (**SAIAC, 2025**). The diplomatic outreach emphasized Indonesia's role as a key strategic partner in Asia-Pacific trade and a stable supplier of essential commodities such as vegetable oils.

The second strategic component emphasized export market diversification. Learning from the hazards of over-reliance on a limited number of destination markets, Indonesia intensified efforts to expand palm oil exports to countries such as India, Pakistan, Brazil, Nigeria, and Egypt. Several of these countries offered tariff-friendly or preferential access arrangements, while others were targeted through accelerated negotiations under Comprehensive Economic Partnership Agreements (CEPA) and Preferential Trade Agreements (PTA) (**Ministry of Trade, 2025**). This geographic rebalancing strategy not only spread risk but also opened opportunities for value-added product positioning in new emerging markets.

Third, the Indonesian government embarked on domestic regulatory reforms, focusing on streamlining and easing non-tariff measures (NTMs) that had previously hindered export efficiency. Two regulations came under particular scrutiny: the Tingkat Komponen Dalam Negeri (TKDN), which required minimum domestic content in certain industries, and Prohibitions and Restrictions, a restrictive import-export licensing scheme. By simplifying documentation processes and integrating trade permitting systems under the Online Single Submission (OSS) platform, Indonesia aimed to reduce logistical frictions and improve responsiveness to shifting global demand.

The fourth pillar encompassed a package of fiscal incentives. Recognizing the cost pressure on exporters following the U.S. tariff shock, the Ministry of Finance introduced several relief programs. These included import duty exemptions, PPN (value-added tax) refund accelerations, and export tax adjustments such as temporary suspension of the crude palm oil (CPO) levy. Such measures were essential in preserving exporter cash flow and

preventing supply disruptions at both the upstream and downstream stages of the palm oil value chain.

The final element of Indonesia's mitigation strategy involved leveraging the services trade deficit with the United States. Despite its goods surplus, Indonesia maintains a sizable deficit in digital services—including payments for U.S.-based cloud platforms, streaming, and fintech services. Policymakers used this imbalance as a basis for negotiating tariff concessions or counterbalancing trade measures, arguing that the overall economic exchange is not as one-sided as goods data suggests. This strategic framing served to neutralize the political justification for the tariff while elevating the discourse to a comprehensive view of bilateral economic relations.

Indonesia's approach reflects broader adaptive trade strategies commonly recommended for emerging economies facing unilateral trade actions (**Hoekman & Kostecki, 2009**). The emphasis on institutional agility, diversification, and domestic efficiency aligns with resilience-building principles endorsed by the World Bank and WTO for small and medium economies exposed to systemic shocks. In Indonesia's case, this strategy is anchored not only in damage control but also in long-term transformation of the palm oil industry.

Among the notable longer-term measures are the government's investments in supply chain traceability technologies, including blockchain-based tracking systems for sustainable palm oil certification (ISPO and RSPO). These systems are designed to meet increasingly strict import requirements in global markets such as the EU and Japan, which are adopting deforestation-free and human rights-compliant sourcing rules. By aligning with international sustainability frameworks, Indonesia seeks to future-proof its palm oil sector against both tariff and non-tariff trade restrictions.

Moreover, Indonesia's mitigation framework demonstrates an integrative approach—bridging trade, fiscal, digital, and regulatory dimensions—underscoring the complexity of modern trade conflicts and the need for multidimensional responses. While short-term relief has stabilized trade flows, long-term competitiveness hinges on continued investment in innovation, sustainability, and institutional reform.

Strategic Implications

The recent imposition of the U.S. reciprocal tariff policy against Indonesia's palm oil exports offers a stark illustration of the inherent structural vulnerabilities faced by export-dependent economies. In particular, it reveals the economic fragility that arises when a nation's external earnings are tied heavily to a limited number of commodities and target markets. Indonesia's reliance on palm oil, which constitutes over 10% of its non-oil-and-gas export revenue, and its historical dependence on markets such as the U.S. and the EU, created significant exposure to unilateral trade shocks (**GAPKI, 2025; BPS, 2025b**). These structural imbalances magnify the impact of external policies and reduce national resilience in periods of geopolitical and economic volatility.

One of the foremost implications of this episode is the urgency of export market diversification. The Indonesian case demonstrates that even historically stable trade relationships can become unpredictable under shifting political climates. As global trade becomes increasingly influenced by protectionist sentiment, emerging economies must avoid overconcentration and expand their reach into untapped or underdeveloped markets. For Indonesia, new trade corridors in Africa, South Asia, and Latin America present viable

alternatives, particularly when pursued alongside bilateral trade agreements such as CEPA and PTA (**Ministry of Trade, 2025**).

Additionally, the disruption triggered by the tariff policy underscores the need for domestic value addition. A significant portion of Indonesia's palm oil exports remain in crude or semi-processed form, leaving the country vulnerable to price fluctuations and foreign non-tariff measures (NTMs). By investing in downstream processing—such as oleochemicals, cosmetics, and biodiesel—Indonesia can capture more of the value chain and reduce its dependency on raw commodity exports. The government's push for industrial upgrading through the palm oil roadmap and the National Industrial Policy 2025 reflects this strategic pivot toward industrial deepening.

Closely related to value addition is the imperative of regulatory coherence and institutional reform. Trade disruptions often reveal hidden inefficiencies within national export systems—ranging from complicated documentation processes to overlapping agency mandates. Indonesia's experience suggests the necessity of harmonizing its trade-related regulations, particularly in areas such as customs facilitation, digital certification, and environmental compliance. The adoption of the Online Single Submission (OSS) platform and revisions to Prohibitions and Restrictions, TKDN regulations were steps in the right direction but need to be part of a broader strategy of regulatory alignment with international norms (**World Bank, 2023**).

At the geopolitical level, this case highlights the importance of assertive trade diplomacy. Countries like Indonesia must not only respond reactively to policy changes but also engage proactively in shaping trade norms and dispute resolutions. Greater participation in multilateral institutions such as the WTO, ASEAN, and the G20—combined with regional leadership through initiatives like the Regional Comprehensive Economic Partnership (RCEP)—can increase Indonesia's leverage in future trade negotiations (**SAIAC, 2025; Hoekman & Kostecki, 2009**). Trade diplomacy must also be equipped with strong data analytics, economic modeling, and legal capabilities to support bargaining positions.

The palm oil tariff episode also offers a lesson in the value of economic forecasting and risk mapping. Given the unpredictability of trade relations, policymakers must institutionalize scenario planning, establish early warning systems, and conduct regular stress tests on key export sectors. Real-time trade monitoring platforms and predictive analytics could provide governments with the necessary intelligence to preempt shocks and deploy interventions promptly (**World Bank, 2023**).

Moreover, this case affirms the need for a whole-of-economy approach to trade resilience. Beyond ministries of trade and industry, responses to external trade shocks should involve ministries of finance, environment, labor, and digital affairs. This coordination ensures that fiscal buffers, sustainability requirements, labor protections, and technology infrastructure are integrated into a unified trade resilience framework (**OECD, 2022**). Finally, the broader implication of this trade conflict is that resilience must be structural, not situational. While reactive measures such as tariff offsetting and market redirection are crucial, they must be embedded within a long-term economic transformation agenda. For Indonesia, this means building a diversified, technology-enabled, and sustainable export base that is capable of adapting to the evolving landscape of global trade governance.

CONCLUSION

The 2025 U.S. reciprocal tariff policy targeting Indonesian palm oil exports illustrates the acute vulnerability of commodity-dependent economies to abrupt shifts in global trade dynamics. The policy triggered a significant decline in export value and volume, disrupted supply chains, compressed margins, and displaced thousands of workers. Indonesia's multi-pronged policy response—including trade diplomacy, fiscal relief, regulatory reforms, and market diversification—offered critical short-term stabilization while laying the groundwork for long-term resilience. However, the episode underscored the urgent need for structural transformation through export diversification, downstream industrial development, and regulatory coherence. Going forward, Indonesia must adopt a more proactive, strategic, and adaptive trade architecture to navigate an increasingly protectionist and complex global economic order.

LIMITATIONS AND FUTURE RESEARCH RECOMMENDATIONS

This study is primarily based on qualitative analysis and secondary data sources from government reports, trade databases, and media publications, which, while comprehensive, may not fully capture firm-level or regional variations within Indonesia's palm oil sector. Moreover, the analysis focuses predominantly on the short-term impacts of the tariff policy, with limited exploration of medium- to long-term macroeconomic consequences, including investment behavior and rural income shifts. Future research should incorporate quantitative econometric modeling to estimate sectoral elasticity, firm resilience, and labor reallocation dynamics. In addition, comparative studies involving other ASEAN palm oil producers—such as Malaysia, Thailand, or the Philippines—could provide deeper insights into differential policy responses and trade resilience strategies in the face of unilateral tariff measures. Exploring the role of sustainability standards and ESG compliance in shaping future market access would also be a valuable extension of this research.

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