

Research/Review

The Free Trade Zone Policy : A Pathway to the Development of a Special Economic Zone in Batam City

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Abstract: Batam City is a national strategic area that has played a significant role in Indonesia's economic growth since the 1970s. Through its Free Trade Zone (FTZ) policy, Batam has successfully attracted significant investment and developed into an export-oriented trading center. However, the implementation of regional autonomy has created institutional dualism between the Batam City Government and the Batam Business Entity (BP Batam), resulting in overlapping authority, regulatory uncertainty, and a decline in regional economic competitiveness. This study aims to analyze regional development policy strategies that align with the vision of the Batam City Long-Term Regional Development Plan (RPJPD) 2025–2045. This study uses a descriptive qualitative approach with data collection techniques through document studies, secondary data, and interviews with key stakeholders. The results indicate that institutional restructuring is an urgent need to eliminate overlapping authority between the central and regional governments. In addition, harmonization of central and regional regulations, strengthening infrastructure, and improving the quality of human resources are strategic steps in Batam's transition from an FTZ to a Special Economic Zone (KEK). To achieve Batam's successful development in the future, inclusive multi-stakeholder collaboration and governance that adapts to global dynamics are needed. A policy strategy based on synergy, regulatory efficiency, and resource readiness is believed to be able to support the achievement of sustainable economic transformation in accordance with the region's long-term vision.

Keywords: Free Trade Zone (FTZ), Special Economic Zone (SEZ), Institutional Dualism, Development Policy, Batam City.

1. Introduction

Based on Law Number 36 of 2000, which replaces Law Number 1 of 2000 concerning Free Trade Zones and Free Ports, it is stipulated that the territory of Riau Islands Province—specifically Batam—is designated as a Free Trade Zone and Free Port (*Free Trade Zone/FTZ*). Within this zone, various economic activities are permitted, including trade, maritime industry, transportation, banking, tourism, and other economic sectors. The formulation of the FTZ regulation for Batam is the result of collaboration between the central government and the regional government of the Riau Islands Province, serving as the legal foundation for its implementation. In identifying the region's competitive advantages, a neo-classical economic approach is applied, considering factors such as local endowments, infrastructure availability, human resource quality, and the role of institutions through policies that support market connectivity. Economic performance within the FTZ area is strongly influenced by the consistency of policies adopted by both the central and local governments, as well as the availability of adequate facilities. The implementation of the FTZ in Batam is directly supervised and managed by the Batam Indonesia Free Zone Authority (*BP Batam*), formerly known as the Batam Authority. However, in practice, the management and authority of BP Batam have often become a source of polemics, sparking conflicts that affect the dynamics of FTZ development (Kurniawan, 2017). Batam City is a strategic area that plays a significant role in both the national and regional economies. Since its initial development by the Batam Authority in the 1970s, Batam has been designed as an industrial and trade zone with an export orientation. Various policies and special incentives, such as the Free Trade Zone (*FTZ*)

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status, have made Batam an investment magnet and an international trade gateway for Indonesia (Yanti, 2021). The development success during the leadership era of B.J. Habibie became a pivotal milestone, demonstrating Batam's potential as a center of national economic growth. In the early 1990s, Batam's economic growth even reached more than 30% per year. With world-class infrastructure, well-organized industrial estates, and a strategic geographic location, Batam has grown into an industrial city with significant contributions to national non-oil and gas exports (Kuncoro, 2005).

Batam development dynamics are not without complex structural challenges. One of the main challenges emerged with the implementation of regional autonomy in 2000, which established the Batam City Government as the local authority. On the other hand, *BP Batam*, as an extension of the central government, continues to exercise its functions. This situation has resulted in institutional dualism, leading to overlapping authorities, bureaucratic conflicts, and legal uncertainties that hinder the smooth flow of investment and development (Zaenuddin, 2023). Various studies, including research by ISEI Batam (2011) and Bappenas reviews, have indicated that institutional dualism between the Batam City Government and *BP Batam* is the root of numerous development issues, ranging from land conflicts, licensing, asset management, to fiscal institutions. Furthermore, investors often face uncertainty regarding land status and convoluted bureaucratic procedures, ultimately diminishing investment interest. Beyond institutional issues, Batam's development challenges also encompass socio-economic concerns, such as rising unemployment, poverty, urbanization, and declining industrial competitiveness (Puspita, 2022).

The designation of Batam City as a *Free Trade Zone (FTZ)* not only brings positive impacts for economic growth but also creates potential threats that must be anticipated. In general, the negative impacts of free trade zones can be classified into two main categories. First, relatively mild impacts, such as capital inflow and outflow issues, excessive incentives granted to foreign investors, and the potential for unfair competition with local businesses. Second, more severe and concerning impacts arise when foreign investors exert significant influence to the extent of pressuring national policies, and even intervening in internal government affairs that previously promised investment incentives (Yealta, 2015). Considering these possible impacts, strict and comprehensive regulations are required from both the Batam City Government and *BP Batam* as the implementing authority. The designed regulations must ensure that the FTZ operates sustainably and equitably, while protecting the region's economic sovereignty from foreign domination (Nuraisyiah, 2019).

2. Literature Review

The policy of developing free trade zones and special economic zones in Indonesia, particularly in Batam City, cannot be separated from the various strategies formulated to support the achievement of national development goals. To understand the direction of such policies, it is necessary to first explain the concepts of policy strategy, the Free Trade Zone (FTZ), and the Special Economic Zone (SEZ), which form the fundamental framework for decision-making at both the central and local government levels. The following section briefly outlines several definitions, theories, and conceptual frameworks relevant to the discussion of FTZ policy transformation towards SEZ development in Batam City.

Policy Strategy

Digitalization At its core, the concept of strategy was originally defined as a means or method to achieve a specific goal. According to Freddy Rangkuti, strategy is a tool used to attain objectives. Hamel and Prahalad argue that strategy refers to actions that are incremental and continuous in nature, developed based on a forward-looking perspective of what customers may expect in the future. Richard L. Daft explicitly defines strategy as an action plan that describes the allocation of resources and various activities to address the external environment, gain competitive advantage, and achieve organizational goals. In essence, strategy is a systematically devised and carefully considered method to reach intended objectives, which can be interpreted as an organized working method designed to facilitate the implementation of activities in order to achieve predetermined goals. Supriyono states that strategy is an integrated and comprehensive plan formulated by an institution, agency, or

organization. According to Marrus, as cited by Umar, strategy is a process of determining top management plans focusing on the organization's long-term goals, along with the development of methods or efforts to ensure those goals can be achieved. Strategy is specifically defined as actions that are incremental and continuous in nature, carried out from the perspective of what customers are expected to demand in the future (Hendika, 2015). The term *policy* is often used interchangeably with goals, programs, decisions, statutes, regulations, proposals, and grand designs (Abdul Wahab, 1997: 2). Essentially, a policy serves as a guideline for action. This guideline may be simple or complex, broad or specific. In line with the meaning of policy articulated by the United Nations, Fredrick (in Islamy, 1998) defines policy as a series of actions proposed by an individual, group, or government within a particular environment, indicating the obstacles and opportunities involved in implementing the proposed policy to achieve certain objectives (Muadi, 2016).

A common misconception assumes that once a policy has been formally enacted by the authorized authority, it will automatically be implemented as intended by its initiator. In reality, the realization of a public policy requires a complex process and goes through multiple stages. Research conducted by Sholih Muadi in 2016 highlights that public policy is a continuous process that does not end at a single stage. In his view, the most crucial aspect in the dynamics of public policy is the policy cycle itself. This cycle includes several key stages, ranging from formulation and implementation to evaluation of the policy (Delpiero, 2021). As policy studies have developed, more scholars have contributed ideas regarding implementation as an integral part of the policy cycle. According to Wahab, the implementation stage begins once the formal instructions for the policy are issued and encompasses various efforts to manage inputs in order to produce outputs or final outcomes that benefit the public. George Edward (2011), as cited by Widodo, views policy as a dynamic process in which various elements are interconnected and influence the course of its implementation. To understand the extent of each element's influence, it is important to identify and study them comprehensively (Subekti, 2017).

Concept of Free Trade Zone

The concept of a *Free Trade Zone (FTZ)* refers to a designated geographic area where goods can be landed, handled, manufactured, or reconfigured, and re-exported without the intervention of customs authorities. Only when the goods are moved to consumers within the country in which the zone is located do they become subject to prevailing customs duties (UNCTAD, 2019). In Indonesia, the FTZ concept has become a vital instrument to strengthen economic resilience and global competitiveness, especially for regions with strategic positions like Batam. Historically, Batam's FTZ has its roots in the 1970s when the Indonesian government identified the island's potential due to its proximity to Singapore and major international shipping lanes (Kurniawan & Santoso, 2017). The island was initially developed as an industrial base, and the FTZ policy facilitated the influx of foreign capital, advanced manufacturing facilities, and skilled labor. This policy direction was later formalized through Law No. 44 of 2007, which reaffirms Batam's status as a Free Trade Zone and Free Port. According to Wahyuni & Astuti (2009), the legal reinforcement through Law No. 44 of 2007 brought a stronger foundation for investors to manage logistics, supply chains, and production lines with minimized bureaucratic hurdles. A *Special Economic Zone (SEZ)*, meanwhile, extends the FTZ concept by adding elements of economic clustering, integrated infrastructure, and sectoral specialization (Zeng, 2016). SEZs are not merely customs-free areas but are designed as comprehensive economic regions with specific incentives, including tax holidays, streamlined licensing processes, and integrated service facilities to attract high-value industries. Law No. 39 of 2009 outlines these principles for SEZs in Indonesia, aiming to create balanced regional development and reduce economic disparities across islands.

Despite the ambitious objectives, the transition from FTZ to SEZ in Batam has generated considerable debate. Fatimah (2022) highlights that many business actors fear losing the legal certainty and fiscal benefits that they have enjoyed for decades under the FTZ regime. This resistance is understandable, given that any changes in tax treatment, customs procedures, or administrative requirements could disrupt established business models. According to Ismail (2021), the shift toward an SEZ framework needs careful policy synchronization to ensure that new regulations do not overlap with the incentives previously guaranteed under FTZ

status. Muzwardi (2017) emphasizes that the Free Trade Zone is not merely a policy tool but a strategic pillar for sustainable economic development. The ultimate goals include structured regional development, increased national and local revenues, large-scale employment opportunities, and technology transfers. These outcomes align with Indonesia's broader vision to become a global production base and logistics hub, as outlined in the National Medium-Term Development Plan (*RPJMN*). Faizasyah (2021) further elaborates that globally, FTZs have common characteristics that also appear in Batam's implementation. First, they serve as manufacturing and logistics nodes, focusing on re-export-oriented production. Second, their strategic location near global trade routes ensures seamless access to international markets. Third, FTZs typically attract large-scale foreign direct investment (*FDI*) due to liberalized trade and fiscal regimes. Fourth, these areas often rely heavily on integrated infrastructure, such as ports, airports, and industrial estates, to support efficient supply chains. Lastly, the regulatory framework is designed to minimize bureaucratic barriers that otherwise discourage investors.

However, these advantages come with challenges. According to Naim (2019), an enclave-like FTZ can inadvertently facilitate illicit trade if not properly managed. The porous nature of zone boundaries, combined with insufficient customs oversight, creates opportunities for smuggling. This is echoed by Handrisal (2021), who found that weak physical demarcation and lack of robust gate control often lead to leakages of goods meant for exclusive circulation within the free zone, such as duty-free cigarettes and luxury items. The governance of FTZs in Indonesia is legally underpinned by Law Number 44 of 2007, which amends Law Number 36 of 2000 through Government Regulation in Lieu of Law (*Perppu*) Number 1 of 2007. This legal framework specifies that the establishment and operation of free trade zones and free ports must follow detailed Government Regulations (*PP*) to ensure accountability and standardization (Septiansyah, 2022). However, gaps in implementation persist. For instance, according to Nasution (2020), overlapping regulations among local, regional, and national authorities often create legal uncertainty for investors operating in FTZs.

In Batam's case, the local implementing body (*BP Batam*) plays a crucial role in regulating business licensing, customs arrangements, and infrastructure development. Nevertheless, coordination among stakeholders is frequently cited as a bottleneck. As noted by Ramli et al. (2018), the lack of synergy between the *BP Batam*, Batam City Government, and central ministries sometimes results in conflicting policies that hinder investment facilitation. Another dimension that requires attention is the alignment of FTZ development with sustainable economic principles. With the rise of global sustainability standards, investors and trading partners increasingly demand adherence to environmental and social governance (*ESG*) criteria. According to Pradana & Aulia (2021), Batam's FTZ must now integrate green industry practices, efficient waste management, and labor welfare standards to remain competitive in attracting responsible investment.

From a macro perspective, UNCTAD (2019) underscores that successful FTZs worldwide are those that continuously innovate their policy framework to respond to shifting global trade dynamics. They evolve from merely offering fiscal perks to becoming innovation-driven clusters that encourage high-tech industries, research and development, and upskilling of the local workforce. This vision resonates with Indonesia's aspiration to transform Batam and other FTZs into drivers of technological progress and digital economy development (Bappenas, 2020). Moreover, the role of digitalization cannot be overlooked. As emphasized by Yusuf & Prasetyo (2023), integrating smart port technologies, digital customs systems, and automated logistics can significantly enhance the operational efficiency of FTZs.

Concept of Special Economic Zone

The strategy for developing *Special Economic Zones (SEZs)* in Indonesia represents an integrated policy to accelerate equitable regional growth while fostering competitive economic clusters that can create high added value for the nation's economy. SEZs are designed not only as industrial enclaves but also as catalysts for technological advancement, skill enhancement, and innovation diffusion in surrounding regions (Zeng, 2016). Indonesia's aspiration to utilize SEZs as engines of national economic growth is supported by its vast natural resources, strategic maritime location, and growing domestic market. As highlighted

by Prasiska (2023), the Riau Islands Province is one of the key priority areas in Indonesia's SEZ roadmap. Its geographical position near Singapore and Malaysia, coupled with direct access to international shipping routes in the Malacca Strait, makes it a competitive base for foreign direct investment (FDI). Investors see Batam and its surrounding islands as attractive due to logistical advantages, established industrial estates, and continuous government support for improving infrastructure.

A *Special Economic Zone* is a broad concept encompassing various specialized economic areas, including Free Trade Zones (FTZs), Export Processing Zones (EPZs), bonded logistics centers, science parks, and other forms of integrated industrial zones. According to Damuri (2015), the SEZ policy framework offers implementing agencies autonomy to manage local governance, fiscal incentives, licensing, and operational standards under central government mandates. This flexibility allows SEZs to adapt quickly to global economic trends and investor demands. Globally, the SEZ model has proven successful in boosting national industrialization and export competitiveness. The experiences of countries like China, Vietnam, and the United Arab Emirates demonstrate that well-managed SEZs can serve as laboratories for economic policy reform and drivers for broader economic transformation (Farole & Akinci, 2011). For Indonesia, SEZs are expected to become magnets for high-value industries such as electronics, digital technology, automotive, petrochemicals, and aerospace, which can generate substantial backward and forward linkages with local economies.

The Indonesian government's vision for SEZ development aligns with its *Masterplan for Acceleration and Expansion of Indonesia's Economic Development (MP3EI)* and the *National Medium-Term Development Plan (RPJMN)*. These policy frameworks underline the importance of building strong industrial bases outside Java to reduce economic disparities between regions (Bappenas, 2020). SEZs thus play a vital role in realizing a decentralized and diversified economic structure by leveraging regional comparative advantages. Currently, the Riau Islands Province hosts three operational SEZs that reflect Indonesia's strategic direction in diversifying its industrial base. The Galang Batang SEZ in Bintan Regency focuses on mineral processing and downstream industrial activities, aiming to add value to Indonesia's rich bauxite resources (Investment Coordinating Board, 2023). The Nongsa Digital Park SEZ in Batam is positioned as a regional hub for digital technology, creative industries, and high-end tourism, targeting partnerships with Singapore's digital ecosystem. Meanwhile, the Batam Aero Technic (BAT) SEZ is Indonesia's first dedicated facility for aircraft *Maintenance, Repair, and Overhaul (MRO)*, which is crucial for supporting the rapidly growing aviation sector in Southeast Asia (Yusuf & Prasetyo, 2023). The designation of an area as an SEZ considers two critical aspects: geographical advantage and the potential of natural resources. Regions close to international trade routes, major shipping lanes, or neighboring countries are prioritized due to their logistical edge, which reduces transportation costs and enhances global connectivity. In addition, the availability of abundant natural resources provides the raw materials necessary for downstream industries within the SEZ (Damuri, 2015). For example, the Galang Batang SEZ capitalizes on abundant bauxite reserves to develop a competitive aluminum processing industry, contributing to import substitution and value-added exports.

However, the success of SEZs is not solely determined by location or resource endowment. Institutional quality, infrastructure readiness, skilled labor availability, and policy coherence are equally decisive factors (Zeng, 2016). According to the World Bank (2020), many SEZs in developing countries struggle to reach their full potential due to weak governance, unclear regulatory frameworks, and limited coordination between central and local governments. Indonesia has addressed some of these challenges by establishing dedicated SEZ Management Boards (*Badan Pengusahaan*) with delegated authority to handle permits, customs, and investment services under a one-stop integrated system. The SEZ concept also functions as a policy laboratory. Damuri (2015) argues that SEZs offer a controlled environment to experiment with market-friendly policies, tax incentives, and regulatory relaxations that may later be scaled up to the broader economy. If proven effective, these innovative approaches can be replicated in other provinces to enhance Indonesia's overall business climate.

To ensure that SEZs remain globally competitive, the Indonesian government continues to refine its incentive packages. For instance, investors in SEZs are eligible for tax holidays

of up to 20 years, customs exemptions for imported capital goods and raw materials, and simplified immigration procedures for foreign workers and experts (Investment Coordinating Board, 2023). These facilities are intended to reduce entry barriers and attract anchor investors who can drive supply chain development and technology transfer. Sustainability is another emerging focus area in SEZ development. According to Pradana & Aulia (2021), incorporating environmental, social, and governance (*ESG*) principles into SEZ operations is essential for attracting responsible investment and meeting international trade requirements. Many global corporations now prefer to invest in industrial zones that demonstrate compliance with environmental standards, renewable energy use, waste management practices, and community development programs.

In the case of Nongsa Digital Park SEZ, the emphasis on the digital economy aligns with Indonesia's broader push toward digital transformation as a pillar of economic resilience (Yusuf & Prasetyo, 2023). By clustering digital companies, data centers, and creative industries, the SEZ aims to create high-skilled jobs for local talent while fostering innovation spillovers to surrounding areas. Furthermore, the Indonesian government recognizes the importance of infrastructure connectivity for SEZ success. According to Kurniawan & Santoso (2017), efficient seaports, airports, roads, and digital infrastructure are prerequisites for attracting and retaining investors. In the Riau Islands, ongoing improvements to Batam's Hang Nadim International Airport and Batu Ampar Port are part of the broader strategy to strengthen the logistics backbone that supports SEZ activities.

3. Proposed Method

This study employs a descriptive qualitative approach to obtain a comprehensive overview of the Free Trade Zone Policy in the development of Batam City. According to Moleong, the qualitative approach is a research method that produces descriptive data in the form of written or spoken words obtained from individuals and observed activities. In short, the qualitative approach is a research method that can generate descriptive data in written and oral formats derived from participants (Endah, 2023). The goal of this method is to provide a thorough understanding of current conditions, events, and phenomena, as well as to address specific issues encountered during the research process. The research technique used in this study is a qualitative approach, which involves the investigation of social phenomena and human problems through inquiry and understanding.

4. Results and Discussion

With the enactment of Law of the Republic of Indonesia Number 53 of 1999, Batam Island was officially designated as Batam City and gained autonomous regional status. This new status brought significant changes to the governance system and administrative structure of the region. However, the implementation of regional autonomy in Batam has led to the emergence of a dualism of authority, whereby the Batam City Government and the Batam Indonesia Free Zone Authority (BP Batam) each exercise overlapping powers and functions. According to research conducted by the Indonesian Economists Association (ISEI) in 2011, this overlapping authority has manifested in various critical areas, including licensing procedures, land management, infrastructure development, asset administration, and other regulatory aspects. Such overlaps have triggered a series of bureaucratic challenges that have directly affected the efficiency and effectiveness of public administration in Batam City. This condition has generated complex problems, such as decreased investor confidence, a decline in foreign and domestic investment inflows, slower regional economic growth, and a weakening of Batam's overall competitiveness in comparison to other economic hubs in Indonesia and Southeast Asia. To address these challenges and to restore Batam's position as a strategic driver of Indonesia's economy, the government introduced the Free Trade Zone (FTZ) scheme as one of the main policy instruments. The FTZ policy was intended to strengthen Batam's appeal in the eyes of foreign and domestic investors by offering various fiscal incentives, tax exemptions, and regulatory flexibility to facilitate industrial activities and cross-border trade.

Global competitiveness, as assessed by the annual *Global Competitiveness Report* of the World Economic Forum, serves as an important benchmark for measuring the prosperity and productivity of a nation or region. According to the Report, a country's economic well-being is largely determined by its productivity, which can be measured by the value of goods and

services produced per unit of labor, capital, and natural resources. For Batam, the FTZ is expected to contribute directly to enhancing national foreign exchange reserves through increased foreign direct investment (FDI), while simultaneously attracting domestic capital to develop robust, export-oriented industries that can compete on the global stage (Kurniawan, 2017). The issue of institutional dualism remains one of the key challenges highlighted by this study. A review of local planning documents and relevant policy analyses confirms that the overlapping authority between the Batam City Government and BP Batam has caused multiple constraints in land administration, licensing consistency, investment procedures, and budget allocation for development projects. This dualism has not only created legal uncertainty but also contributed to delays in strategic decision-making processes, thereby diminishing Batam's attractiveness as an investment destination. The findings of ISEI Batam (2011) and more recent studies reinforce this view, indicating that persistent bureaucratic conflicts have resulted in inefficient implementation of public policy, administrative confusion, and a lack of clarity in accountability lines (Zaenuddin, 2023).

From an economic perspective, the impact of institutional dualism is particularly evident in Batam's declining growth performance. Statistical data from BPS Batam City (2023) shows a marked slowdown in economic growth over recent years, with the growth rate dropping from 6.7% in 2016 to only 4.2% by 2022. This downward trend is widely attributed to policy uncertainty, especially concerning industrial land governance, inconsistent licensing regimes between central and regional authorities, and ineffective coordination among institutions involved in strategic projects. These obstacles have slowed the execution of key infrastructure projects and delayed improvements in essential public services, which are crucial for sustaining economic expansion and social welfare (Florenca, 2023). In response to these challenges, the development of a Special Economic Zone (SEZ) in Batam City has been positioned as a strategic policy alternative aimed at revitalizing the city's economic performance. The SEZ initiative seeks to address the structural weaknesses of the FTZ scheme by providing a more integrated and comprehensive framework that combines fiscal and non-fiscal incentives with streamlined regulations, improved governance mechanisms, and more targeted sectoral development. Batam's unique geographic position, situated between Singapore and Malaysia and along major international shipping routes, remains one of its most significant strategic advantages. With active ports, modern transportation networks, and direct access to global markets, Batam has the potential to serve not only as Indonesia's western economic gateway but also as a critical logistics and industrial hub within the broader Southeast Asian region.

The transition from the FTZ to the SEZ concept marks an important shift in Batam's economic trajectory. While the FTZ emphasized duty-free trade and minimal customs restrictions, the SEZ provides broader economic benefits by offering enhanced tax incentives, streamlined licensing procedures, and greater legal certainty for investors. This integrated approach is expected to stimulate the development of strategic industries such as high-tech manufacturing, integrated maritime services, advanced logistics, and sustainable tourism. Moreover, the SEZ framework is designed to support long-term regional competitiveness by ensuring that infrastructure development keeps pace with industrial growth. The government has prioritized improvements in port and airport facilities, expansion of road and rail networks, and the provision of reliable energy, water, and telecommunications infrastructure. Equally important is the development of human capital. The government and local stakeholders are actively promoting vocational training and industry-relevant education programs to prepare Batam's workforce for the demands of the modern industrial era and the challenges of Industry 4.0. The goal is to equip the younger generation with the skills and competencies required to support advanced industrial operations and attract high-value investments (Citra, 2020).

Nevertheless, the proposed shift from the FTZ to the SEZ in Batam has sparked significant resistance among local business stakeholders. The Indonesian Employers Association (APINDO) of the Riau Islands Province has raised concerns that the SEZ model could disproportionately benefit government authorities or specific political regimes, while providing fewer tangible advantages for local entrepreneurs. Critics argue that the SEZ's geographically limited scope, which covers only selected areas, contrasts sharply with the broader FTZ, which applied to nearly all of Batam's islands. Moreover, the imposition of Value Added Tax (VAT) and Luxury Goods Sales Tax (PPnBM) within Batam's SEZ is

viewed as undermining the city's long-standing preferential status as a free trade hub bordering Singapore and Malaysia.

This perceived erosion of Batam's unique competitive edge has led to tensions between the local government and the business community. The lack of a mutually acceptable 'win-win solution' has fueled skepticism among local entrepreneurs regarding the future of domestic and foreign investment in Batam. If left unresolved, this discord could weaken collaboration efforts and reduce investor optimism, which in turn may dampen Batam's economic prospects. Therefore, it is crucial for policymakers to establish constructive dialogue with business stakeholders and local communities to design regulatory frameworks that ensure legal certainty while balancing the interests of all parties involved. Through transparent governance and inclusive policy-making, Batam can maintain its relevance as a key driver of Indonesia's economic growth while achieving sustainable and equitable development outcomes (Alfriandi, 2020).

5. Conclusions

Based on the findings and the discussions presented in the previous sections, it can be concluded that the designation of Batam City as a Free Trade Zone (FTZ), formalized through Law Number 36 of 2000, has served as a significant milestone in driving regional economic growth, attracting foreign direct investment (FDI), and strengthening Batam's position as an export-oriented industrial and commercial hub. The FTZ policy framework offered a range of fiscal incentives and regulatory flexibilities that, for decades, made Batam an attractive destination for domestic and international investors. However, throughout its implementation, the governance of Batam has faced persistent structural challenges, most notably the dualism of authority between the Batam City Government and the Batam Indonesia Free Zone Authority (BP Batam). This dualism has created overlapping mandates in crucial areas such as licensing, land management, and regulatory enforcement. As a consequence, the region has witnessed recurring administrative inefficiencies, legal uncertainties, and fragmented decision-making processes, all of which have contributed to a decline in investor confidence, a slowdown in economic growth, and underutilization of Batam's full economic potential.

To address these issues and revitalize Batam's competitiveness in the face of increasing global economic competition, the Indonesian government introduced the policy of transforming the FTZ into a Special Economic Zone (SEZ). This transformation aims to provide a more structured incentive scheme, focus on strategic sectors, and promote industrial clustering and integration. The SEZ is designed to offer a broader range of fiscal and non-fiscal benefits, along with streamlined licensing, modern infrastructure, and legal certainty to attract higher-value investments. Nevertheless, the transition from FTZ to SEZ in Batam has received mixed responses from local stakeholders, especially the business community. On the one hand, the SEZ is viewed as a strategic step towards creating more competitive, sector-specific industrial zones that can adapt to global market demands. On the other hand, local entrepreneurs have voiced concerns about the potential loss of operational flexibility, the restriction of incentive coverage to specific geographical areas, and the imposition of Value Added Tax (VAT) and Luxury Goods Sales Tax (PPnBM), which they fear could erode Batam's unique advantages as a duty-free zone and diminish its competitiveness compared to its previous FTZ status.

Without strong collaboration, clear communication, and a shared commitment to develop fair, transparent, and inclusive regulations, the shift from FTZ to SEZ risks exacerbating existing governance conflicts and further undermining investor confidence. Therefore, a comprehensive policy strategy is needed one that does not focus solely on fiscal incentives and physical infrastructure but also prioritizes legal certainty, bureaucratic efficiency, and the empowerment of local human resources. It is equally vital to align the diverse interests of all stakeholders through participatory dialogue and collaborative policymaking. By doing so, Batam can ensure that its economic transformation progresses in an inclusive, sustainable, and competitive manner, ultimately securing its role as one of Indonesia's leading gateways for investment and international trade in the long term.

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