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**NO. 338**

**FROM COMPETITION TO COOPERATION:  
THE GLOBAL PALM OIL “SUSTAINABILITY  
TURN” AS A TURNING POINT FOR THE  
MALAYSIA-INDONESIA  
“SPECIAL RELATIONSHIP”**

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## **Abstract**

Palm oil is the source of a common identity between Malaysia and Indonesia, the two largest palm oil producers globally. As with many other socio-cultural aspects of the Malaysia-Indonesia “special relationship”, palm oil has also led to heightened competition between both nations. However, recent negative sentiments towards palm oil originating from sustainability-conscious markets in the north have threatened both states’ access to important export markets. This paper examines how these developments have marked an important turning point in Malaysia-Indonesia relations. Faced with such external pressures, both states are now increasingly reliant on each other’s continued prominence for their own market survival — their shared strategic interests tending to facilitate cooperation instead of conflict or competition. This paper takes the Malaysian perspective in illustrating the shift from competition to cooperation within the palm oil sector. Of particular interest are the issues over transboundary haze, where Malaysia’s responses have been increasingly geared towards appeasement, restrained by concerns about related fallouts in the palm oil sector.

## Introduction

Indonesia and Malaysia are two of the world's largest palm oil producers, producing 58% and 26% of all palm oil, respectively.<sup>1</sup> The palm oil sectors in both countries have a long history of interlinkages and interdependence that continue to the present day. Despite this, relations over palm oil have traditionally remained at arms-length and mildly rivalrous, with both countries striving to maintain their respective positions as the largest producers and exporters in this lucrative market. In this paper, we shall examine the current period as a turning point in Malaysia-Indonesia relations, and their "special relationship" over palm oil.

Negative sentiments towards palm oil originating from sustainability-conscious markets in the north have tainted perceptions of the sector as a whole, which affects both countries equally. As this "sustainability turn" affects the Malaysia-Indonesia "special relationship", the increasingly "equal" material capacity of both countries in the palm oil sector coupled with "outsider"<sup>2</sup> (outside the context of the Malaysia-Indonesia relationship) pressure towards palm oil sustainability has progressively reframed the issue as one of common strategic interests. Hence, both states are now increasingly reliant on each other's continued prominence for their own market survival. While this was less obvious when the pressure came largely from consumers, this paper argues that once these pressures began to take the very real form of actual policy impacts, conflict and competition would give way to cooperation as both states adopt similar strategic outlooks.

This paper contributes to the study of Indonesia-Malaysia relations by focusing on palm oil as a possible point of cooperation instead of contention. We begin with a review of the literature surrounding the concept of the Malaysia-Indonesia "special relationship", before taking a Malaysian perspective to analysing the evolution of the bilateral relations in the context of palm oil and haze. Next, we outline how palm oil was previously viewed as a source of strategic competition between both countries, before detailing how recent policy-level global anti-palm oil developments have encouraged Malaysia to move from competitiveness and differentiation towards cooperation with Indonesia. The paper then delves into how Malaysia's responses to transboundary haze have been increasingly geared towards appeasement, restrained by concerns about related fallouts in the palm oil sector. Finally, we conclude by showing how a higher focus on shared strategic interests may be the most critical way forward for Malaysia and Indonesia to reap greater tangible benefits from their "special relationship".

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<sup>1</sup> "Palm oil industry worldwide," Statista, 2020c

<sup>2</sup> Khalid, K., and Yacob, S., "Managing Malaysia-Indonesia relations in the context of democratization: The emergence of non-state actors," *International Relations of the Asia-Pacific* 12, no. 3 (2012): 355–387, <https://doi.org/10.1093/irap/lcr024>.

## The Malaysia-Indonesia “Special Relationship”

Special relationships between states can be formed over common identities and shared strategic interests, resulting in substantial cooperation or substantial conflict and competition.<sup>3</sup> In general, the “special relationship” between Malaysia and Indonesia is characterised by the common identity arising from a shared language, culture, and religion (*serumpun*).<sup>4</sup> Because of this, the “emotional” dimension often has a deep influence on the relationship: fostering expectations of mutual understanding and deference that, when unfulfilled, could lead to bitter disputes.<sup>5</sup> One example is the regular diplomatic tiffs over transboundary haze.<sup>6</sup>

On the other hand, shared strategic interests mean that both states rely on each other’s presence for survival. This tends to facilitate cooperation instead of conflict.<sup>7</sup> In such cases, both states need to own an equitable amount of power or material capacity to shape a similar strategic outlook on “common” interests. However, rather than being viewed as equals, Indonesia traditionally sees itself as the “big brother” (*abang*) to Malaysia’s “small brother” (*adik*) due to its physical and population size, cultural legacy, and geopolitical preponderance. Meanwhile, Malaysia’s status as the more developed and prosperous nation has led to an implicit rivalry. Indonesia is often seen as playing catch-up in its quest for economic equalisation with its neighbour.<sup>8</sup> Scholars have noted points of contention within the Malaysia-Indonesia relationship marked by divergent strategic interests and hierarchy, leading to conflict and competition.<sup>9</sup> These include the ongoing illegal immigrant and foreign workers issues as well as high-profile bilateral issues like the Ambalat and Sipadan-Ligitan territorial disputes.<sup>10</sup>

Many researchers have explored the migration issues between the two countries in detail. Spaan et al.<sup>11</sup> traced the evolution of Malaysian policy (from an open and welcoming policy post-independence to strengthen the Malay position, to becoming a more closed one) and its impact on Indonesian immigrants. The reasons for this shift have been identified as ranging from the increase in clandestine immigration and perceptions of criminal tendencies among Indonesians,<sup>12,13</sup> to changes in

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<sup>3</sup> Ho, Y. C., “Examining the Concept of a Special Relationship: A Study of Indonesia-Malaysia Relations,” *The Asian Conference on the Social Sciences*, 2016.

<sup>4</sup> Wardhani, B. L. S. W., “Indonesia-Malaysia Relations in the Post-Confrontation Era: the Role of the Serumpun Concept,” *Masyarakat, Kebudayaan Dan Politik* 12, no. 3 (1999): 25–44.

<sup>5</sup> Khalid, K., and Yacob, S., (2012), op. cit.

<sup>6</sup> Clark, M., and Pietsch, J., “9. Uneasy Neighbours: Indonesia-Malaysia Relations under Yudhoyono,” in *Aspirations with Limitations* (January 2019), 176–204, <https://doi.org/10.1355/9789814786973-010>.

<sup>7</sup> Ho, Y. C., (2016), op. cit.

<sup>8</sup> Khalid, K., and Yacob, S., (2012), op. cit.

<sup>9</sup> Ho, Y. C., (2016), op. cit.

<sup>10</sup> Wardhani, B. L. S. W., (1999), op. cit.

<sup>11</sup> Spaan, E., Van Naerssen, T., and Kohl, G., “Re-imagining borders: Malay identity and Indonesian migrants in Malaysia,” *Tijdschrift Voor Economische En Sociale Geografie* 93, no. 2 (2002): 160–172, <https://doi.org/10.1111/1467-9663.00192>.

<sup>12</sup> Liow, J., “Desecuritisising the ‘Illegal Indonesian Migrant Worker’ Problem in Malaysia’s Relations with Indonesia,” *IDSS Commentaries*, no. 17 (2002): 1–5, <http://www.rsis.edu.sg/wp-content/uploads/2014/07/CO02018.pdf>.

<sup>13</sup> Liow, J., “Malaysia’s illegal Indonesian migrant labour problem: In search of solutions,” *Contemporary Southeast Asia* 25, no. 1 (2003): 44–64, <https://doi.org/10.1355/CS25-1C>.

identity consciousness (from *Nusantara*-based “Malayness” towards “Muslimness”, which reduces an Indonesian to a “mere” foreign Muslim, just like a Bangladeshi or Pakistani).<sup>14</sup> Despite the “web of transnationalised social relations of reproduction” linking both states as described by Elias (2013),<sup>15</sup> migration is seen as a potent example of the politicisation of hierarchy in the Malaysia-Indonesia “special relationship”. Malaysia’s higher economic development and employment opportunities have been the main cause of Indonesian labour migration,<sup>16</sup> which Liow (2002, 2003)<sup>17,18</sup> argues has led to securitisation of the issue and a lack of political will for compromise on the part of both Indonesia and Malaysia. This includes migration within the palm oil sector, which is also seen in the work by Fathana (2018)<sup>19</sup> and Lindquist (2017),<sup>20</sup> who have explored how increased demand for workers in the Malaysian palm oil sector has impacted migration infrastructure and bilateral relations.

Scholars like Butcher (2013),<sup>21</sup> Druce & Baikoeni (2018),<sup>22</sup> Dunan & Adnan (2014),<sup>23</sup> and Puryanti & Husain (2011)<sup>24</sup> have, in turn, focused on border issues. Druce & Baikoeni (2018) have described the Ambalat issue as “the most controversial issue between the two countries since *konfrontasi*”, while Butcher (2013) has described how the Sipadan-Ligitan dispute is of particularly high stakes for both countries. A study by Dunan & Adnan (2014) detailed how the Indonesian media has regularly framed Malaysia as a little brother who did not “appreciate the sibling relationship” when covering the Ambalat issues, while Wardhani’s (1999)<sup>25</sup> work detailed Indonesia’s view of Malaysia as not being “thoughtful towards the Indonesian government” in the Sipadan-Ligitan conflict. However, while these issues remain unresolved, Malaysia and Indonesia have managed to mitigate their incompatibilities and avoid conflict,<sup>26</sup> something which Fauzan (2016)<sup>27</sup> had argued to be at least partially due to the influence of the *Nusantara* and “*abang-adik*” concepts in Indonesian approaches to border management. Puryanti & Husain (2011) have shown how these border dynamics played out on

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<sup>14</sup> Spaan, E., Van Naerssen, T., and Kohl, G., (2002) op. cit.

<sup>15</sup> Elias, J., “Foreign policy and the domestic worker,” *International Feminist Journal of Politics* 15, no. 3 (2013): 391–410, <https://doi.org/10.1080/14616742.2012.755835>.

<sup>16</sup> Spaan, E., and van Naerssen, T., “Migration decision-making and migration industry in the Indonesia-Malaysia corridor,” *Journal of Ethnic and Migration Studies* 44, no. 44 (2018): 680–695, <https://doi.org/10.1080/1369183X.2017.1315523>.

<sup>17</sup> Liow, J., (2002), op. cit.

<sup>18</sup> Liow, J., (2003), op. cit.

<sup>19</sup> Fathana, H., “Palm Oil Politics In Malaysia And Indonesia: Competition Or Collaboration?” *Journal of Southeast Asian Studies* 23, no. 2 (2018): 47–64, <https://doi.org/10.22452/jati.vol23no2.3>.

<sup>20</sup> Lindquist, J., “Brokers, channels, infrastructure: moving migrant labor in the Indonesian-Malaysian oil palm complex,” *Mobilities* 12, no. 2 (2017): 213–226, <https://doi.org/10.1080/17450101.2017.1292778>.

<sup>21</sup> Butcher, J. G., “The international court of justice and the territorial dispute between Indonesia and Malaysia in the Sulawesi Sea,” *Contemporary Southeast Asia* 35, no. 2, (2013): 235–257, <https://doi.org/10.1355/cs35-2e>.

<sup>22</sup> Druce, S., and Baikoeni, E. Y., “Circumventing Conflict: The Indonesia-Malaysia Ambalat Block Dispute,” in *Contemporary Conflicts in Southeast Asia: Asia in Transition*, (Singapore: Springer, 2018), 137–156, <https://doi.org/10.1007/978-981-10-0042-3>.

<sup>23</sup> Dunan, A., and Adnan, H. M., “Is Malaysia Little Brother of Indonesia? A Framing Analysis of Ambalat Conflict,” *Sosio Humanika* 7, no. 1 (2014): 1–8.

<sup>24</sup> Puryanti, L., and Husain, S. B., “A people-state negotiation in a borderland: A case study of the Indonesia-Malaysia frontier in Sebatik Island,” *Wacana, Journal of the Humanities of Indonesia* 13, no. 1, (2011): 105, <https://doi.org/10.17510/wjhi.v13i1.11>.

<sup>25</sup> Wardhani, B. L. S. W., (1999), op. cit.

<sup>26</sup> Druce, S., and Baikoeni, E. Y. (2018), op. cit.

<sup>27</sup> Fauzan, F., “The Dynamism of *Nusantara* and *Adik-Abang* Concepts in Managing Border Areas of Indonesia-Malaysia,” *Proceedings of the 5th International Conference on International Studies (ICIS)*, March 2014.

the ground in Pulau Sebatik, an island off Borneo that is split almost equally between Indonesia and Malaysia.

While previous works have mainly focused on common identities (language, culture, religion) as the main source of closeness between the two neighbours, this paper focuses on their strategic interests as major palm oil trading nations. Furthermore, while previous studies have largely focused on internal pressures like territorial sovereignty and socioeconomic hierarchy in explaining the conflictual and competitive outcomes despite (and because) of the common identities, this paper considers the extent to which pressures from “outside”<sup>28</sup> this special relationship can produce different outcomes. Taken together, this paper argues that similar external pressures faced by both countries have reshaped an area of conflicting strategic interests into a common one, complementing the existing common identities and promoting cooperative outcomes.

## **Palm Oil as a Source of Strategic Competition**

The African oil palm (*Elaeis guineensis*) was first brought to Southeast Asia in 1848. The Bogor (then Buitenzorg) Botanical Gardens in Java was the entry point for oil palm into Indonesia (then the East Indies).<sup>29</sup> It was then brought to Malaysia (then Malaya) as an ornamental plant in 1870. The cultivation of palm oil as a commercial crop began in the East Indies in 1911 and in Malaya in 1917. By 1937, the East Indies was the world’s largest exporter of palm oil.

### ***Strategic Importance of Palm Oil***

In both countries, most commercial plantations belong to state-owned enterprises or well-connected private companies (both local and transnational) — around 61% and 59% in Malaysia and Indonesia, respectively. Their close connections have allowed for preferential access to land for cultivation. This has led to many land conflicts with surrounding forest-dependent communities or smallholders<sup>30</sup> in Indonesia and, to a lesser extent, in Malaysia.

Palm oil is viewed as an engine of social mobility in both countries and has been credited for lifting thousands of rural Malaysians and Indonesians out of poverty. In Indonesia, the industry employs about 20 million Indonesians, both directly and indirectly.<sup>31</sup> Palm oil is a key crop in Indonesia’s *transmigrasi* programme, which spans the period before independence until the present times. The

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<sup>28</sup> Khalid, K., and Yacob, S., (2012), op. cit.

<sup>29</sup> Baudoin, A., Bosc, P. M., Bessou, C., and Levang, P., “A Short History of Palm Oil in Indonesia: A ‘success story’,” in *Review of the Diversity of Palm Oil Production Systems in Indonesia: Case Study of Two Provinces: Riau and Jambi* (2017), 1–6. [www.jstor.org/stable/resrep16293.4](http://www.jstor.org/stable/resrep16293.4).

<sup>30</sup> Abram, N. K., Meijaard, E., Wilson, K. A., Davis, J. T., Wells, J. A., Ancrenaz, M., Budiharta, S., Durrant, A., Fakhruzzki, A., Runting, R. K., Gaveau, D., and Mengersen, K., “Oil palm-community conflict mapping in Indonesia: A case for better community liaison in planning for development initiatives,” *Applied Geography* 78, (2017): 33–44, <https://doi.org/10.1016/j.apgeog.2016.10.005>.

<sup>31</sup> Varkkey, H., Tyson, A., and Choiruzzad, S. A. B., “Palm oil intensification and expansion in Indonesia and Malaysia: Environmental and socio-political factors influencing policy,” *Forest Policy and Economics* 92, (2018): 148–159, <https://doi.org/10.1016/j.forpol.2018.05.002>.

programme aims to reduce the population pressure on Java island and develop food-crop production in the outer islands. Together with the locals, these transmigrants formed the target group for *Perkebunan Inti Rakyat* (PIR or Nucleus Estate and Smallholders) and PIR-Trans schemes launched in 1978, where smallholders are allocated two-hectare plots within the periphery (“plasma”) of commercial plantations (“nucleus”).<sup>32</sup> In Malaysia, palm oil is also a key crop in the Malaysian government’s organised land collectives, designed as “catch up” vehicles for the poorer Malay and Bumiputera communities. FELDA is the oldest and best known. Under FELDA, each family was given land to cultivate under an organised smallholder system. FELDA smallholders are now responsible for about 710,000 hectares (12.3%) of all palm oil land in the country.

FELDA settlers were seen as vote banks for Barisan Nasional (BN), Malaysia's ruling party, from independence until 2018. Thus, maintaining high productivity in these settlements is a political priority. The Malaysian government set up the Palm Oil Research Institute of Malaysia (PORIM), later known as the Malaysian Palm Oil Board (MPOB) in 1974. MPOB developed high-yielding seed varieties and tissue cultures and ascertained ideal levels of nutrients and fertilisers to improve the productivity of the plants. This knowledge and raw materials are shared with FELDA settlers and other smallholders around Malaysia by *Tunjuk Ajar dan Nasihat Sawit* (TUNAS) officers stationed in all major grower cities. Commercial plantations also maintain advanced R&D facilities, which, when taken together with MPOB’s efforts, resulted in a national average of 21 tonnes of fresh fruit bunches (FFB) per hectare, compared to 17 tonnes per hectare in Indonesia (see Figure 1). While Indonesia has its own R&D arm in the Indonesia Oil Palm Research Institute (IOPRI), technical advancements have been less pronounced than MPOB. The dissemination of seedlings and know-how to Indonesian smallholders is further complicated by decentralisation.<sup>33</sup>

**Figure 1: Efficiency Comparisons between Malaysia and Indonesia<sup>34</sup>**

Parameters	Malaysia	Indonesia
Planted area	5.2 mil hectares (See Chart 1)	12.3 mil hectares (See Chart 2)
National Annual Yield	21 t per hectare of fresh fruit bunches (FFB)	17 t per hectare of FFB
Mature/Immature	86%/14%	75%/25%
Share of World Market	41%	46%
Types of Production	61.2% on private estates, 22.5% on organised smallholder land (including FELDA, FELCRA, RISDA and state agencies), 16.3% on independent smallholder land	53% of on private estates, 6% on state-owned company land, 8.6% on plasma smallholder land, 32.4% on independent smallholder land

Since the Southeast Asian palm oil boom in the 1990s, palm oil has been identified as a strategic crop for economic growth and modernisation in both Malaysia and Indonesia. Palm oil was identified as a National Key Economic Area in Malaysia’s Economic Transformation Programme (ETP), launched in 2010. The Ministry of Primary Industries and Commodities is broadly in charge of palm oil matters and has been informally known as the “Ministry of Palm Oil”. In Indonesia, palm oil has been identified as a strategic sector at the presidential level, with various administrations creating special taskforces to oversee industry sustainability and reform: the Presidential Delivery Unit for Development

<sup>32</sup> Baudoin, A., Bosc, P. M., Bessou, C., and Levang, P., (2017), op. cit.

<sup>33</sup> Varkkey, H., Tyson, A., and Choiruzzad, S. A. B., (2018), op. cit.

<sup>34</sup> Ibid.

Monitoring and Oversight (UKP4) under Yudhoyono, and the Presidential Staff Office (KSP) under Jokowi.<sup>35</sup>

Palm oil is the fourth largest component of the Malaysian economy and its largest agricultural sector, contributing 38% of Malaysia's agricultural output value.<sup>36</sup> It has steadily contributed about 3% of Malaysia's GDP, with RM38.24 billion contributed in 2019.<sup>37</sup> Palm oil is Indonesia's largest agricultural export and contributes around 4.5% to 7% of Indonesian GDP annually.<sup>38</sup> Malaysia was the largest producer of palm oil in the world until Indonesia overtook it in 2008. However, it remains the world's largest exporter while Indonesia's local palm oil consumption remains higher than Malaysia's.

### ***Conflicting Strategic Interests Leading to Competition***

Both countries' palm oil sectors are closely interlinked. However, this interdependence was mainly informed by concepts of hierarchy: Indonesia relies on foreign investors from Malaysia, and Malaysia relies on foreign workers from Indonesia.

While the Indonesian palm oil sector post-independence stagnated due to limitations in foreign investment during Sukarno's leadership, the aftermath of the Asian Financial Crisis and IMF involvement saw the reopening of the sector in 1997-8. Incoming investment, largely by major Malaysian plantations encouraged by land scarcity back home, played a key role in the bounce-back of the sector in Indonesia.<sup>39</sup> Malaysian plantation investors were especially adept at navigating the business landscape in Indonesia as both countries shared a similar corporate culture based on patronage. They could insert themselves into existing patronage networks there, allowing them preferential access to lands and licenses while banking upon existing patron-client networks at home for protection, for example, when accused of being complicit in fires in Indonesia.<sup>40</sup>

The Malaysian government also sponsored the establishment of a low-profile but influential Jakarta-based lobby group, the Association of Oil Palm Plantation Investors of Malaysia in Indonesia (APIMI), in 1999. APIMI is among the few industry groups that attend the yearly bilateral economic talks between Malaysia and Indonesia and have been known to directly raise issues of concern with the leaderships of both countries.<sup>41</sup> Malaysian companies are now the largest group of foreign investors in

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<sup>35</sup> Choiruzzad, S. A. B., Tyson, A., and Varkkey, H., "The ambiguities of Indonesian Sustainable Palm Oil certification: internal incoherence, governance rescaling and state transformation," *Asia Europe Journal* 19, no. 2 (2021): 189–208, <https://doi.org/10.1007/s10308-020-00593-0>.

<sup>36</sup> Chang, F. K., "Palm Oil: Malaysian Economic Interests and Foreign Relations," Foreign Policy Research Institute, April 12, 2021, [www.fpri.org/article/2021/04/palm-oil-malaysian-economic-interests-and-foreign-relations/](http://www.fpri.org/article/2021/04/palm-oil-malaysian-economic-interests-and-foreign-relations/).

<sup>37</sup> "Palm oil industry in Malaysia," Statista, 2020b.

<sup>38</sup> Varkkey, H., Tyson, A., and Choiruzzad, S. A. B., (2018), *op. cit.*

<sup>39</sup> Choiruzzad, S. A. B., Tyson, A., and Varkkey, H., (2021), *op. cit.*

<sup>40</sup> Varkkey, H., *The Haze Problem in Southeast Asia - Palm oil and patronage* (Routledge, 2016).

<sup>41</sup> *Ibid.*

the Indonesian palm oil sector.<sup>42</sup> A study by consultancy group Aidenvironment concluded that Malaysian interests owned at least 1.8 million hectares of oil palm land bank in Indonesia in 2013 (see Figure 2), which works out to about 17% of Indonesia’s total oil palm plantation area.<sup>43</sup>

Figure 2: Top Four Malaysian Company Groups’ (>100,000 hectares) Aggregate Oil Palm Land Bank in Indonesia, 2013<sup>44</sup>

No	Malaysian groups	Land bank
1	Minamas Gemilang (Sime Darby)	289,000
2	Genting Plantations	193,000
3	KLK	120,000
4	TSH Resources	109,000

In turn, in Malaysia, plantations are highly reliant on Indonesian labour. This fits into the broader trend of Malaysian reliance on Indonesian labour for jobs considered “dirty, difficult, and dangerous” (3D). Malaysia relies on foreign workers for over 80% of its plantation workforce. Of these, 80%–90% were Indonesian citizens working mainly as FFB harvesters and collectors, with more working in palm oil mills and refineries.<sup>45</sup> There is a further undocumented number — workers who are likely to have crossed over Borneo’s porous East Malaysia-Kalimantan border illegally, with some settling in Malaysia permanently.

Hence, despite sharing a strategic interest in palm oil, this did not result in substantial cooperation between the world’s two largest palm oil producers. Instead, a mildly rivalrous relationship took shape, with both countries competing to maintain their respective positions as the leading producers and exporters of this lucrative commodity. In the mid-1980s, the Indonesian government formulated a specific policy goal to overtake Malaysia as the world’s largest palm oil producer, which it achieved in 2008 (arguably due to the boom created by Malaysian investments).<sup>46</sup>

Campaigns like the MPOC advertisement promoting Malaysian palm oil as “sustainable since 1917” (which was subsequently banned by the UK Advertising Standards Authority in 2009) were among Malaysia’s efforts to differentiate its palm oil from its neighbour. And despite a 1997 bilateral treaty where the Indonesian government allocated 1.5 million hectares to Malaysian investors to develop oil palm estates in 1997,<sup>47</sup> there were calls in the Indonesian parliament in 2014 to limit Malaysian ownership of palm oil plantations in Indonesia, which were viewed to be in direct competition

<sup>42</sup> “Malaysian Overseas Foreign Direct Investment in oil palm land bank: Scale and sustainability impact,” Aidenvironment, 2014.

<sup>43</sup> “Palm oil industry in Indonesia,” Statista, 2020a.

<sup>44</sup> Aidenvironment, 2014, op. cit.

<sup>45</sup> Ismail, A., “The Effect of Labour Shortage in the Supply and Demand of Palm Oil in Malaysia,” *Oil Palm Industry Economic Journal* 13, no. 2 (2013): 15–26.

<sup>46</sup> Varkkey, H., Tyson, A., and Choiruzzad, S. A. B., (2018), op. cit.

<sup>47</sup> Varkkey, H., (2016), op. cit.

with Indonesian-owned plantations.<sup>48</sup> There has also been a long-running “tariff war” between the countries over palm oil. When commodity prices for palm oil dropped in 2014, the Malaysian government eliminated export tariffs for crude palm oil (CPO) to boost its sales. Indonesia retaliated soon after with a similar zero-tax regime.<sup>49</sup>

Indonesia has been known to restrict migrant worker supply to Malaysia following cases of mistreatment. Plantation workers have complained of retrenchment and job irregularity, non-payment of legal wages, heightened risk of forced overtime, and lack of access to personal protective equipment. Undocumented workers have complained of inhumane conditions in detention centres.<sup>50</sup> Foreign labour translates directly to productivity: the hardening of borders to foreign workers due to COVID-19 in 2020 caused Malaysian palm oil yield to drop as much as 25%.<sup>51</sup>

Conflict over seasonal transboundary air pollution known as “haze” also feeds into competition over palm oil. While similar land-use change practices drive peat fires in both countries, meteorological patterns and the much larger scale of fires in Indonesia mean that Malaysia is often also affected by transboundary haze from Indonesia alongside localised haze. During the annual haze season, both countries would often descend into spats of finger-pointing. While Malaysia would raise concerns about the haze originating from Indonesia affecting Malaysians, Indonesia would often retaliate by naming and shaming Malaysian palm oil companies operating in Indonesia linked to the fires there. Indeed, one of the earliest successful prosecutions in Indonesia for haze-producing fires was the high-profile case of PT Adei Plantation and Industry, a subsidiary of the Malaysian company KLK.<sup>52</sup>

## Palm Oil and Sustainability Concerns

The oil palm is the world’s most efficient oil crop. It only takes 0.26 hectares of planted land to produce one tonne of palm oil, compared to rapeseed (1.25 hectares), sunflower (1.43 hectares), and soybean (2 hectares). Because of this, the palm oil sector produces 35% of all vegetable oil on less than 10% of the land allocated to oil crops globally.<sup>53</sup> This efficiency, alongside low mechanisation and cheap labour, makes palm oil the cheapest vegetable oil. Furthermore, its stable physical and chemical properties facilitate its widespread use in foodstuff, cosmetics, pharmaceuticals, oleochemicals, and biofuels. A WWF report estimated that it is used in about 50% of all the packaged products found in supermarkets.<sup>54</sup>

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<sup>48</sup> Varkkey, H., Tyson, A., and Choiruzzad, S. A. B., (2018), op. cit.

<sup>49</sup> Fathana, H., (2018), op. cit.

<sup>50</sup> “COVID-19 and Migrant Agriculture Workers in the Palm Oil Sector in Malaysia: Recommendations for Protecting Workers,” Fair Labor Association, July 2020, [www.fairlabor.org/projects/covid-19-and-migrant-agriculture-workers-in-the-palm-oil-sector-in-malaysia/](http://www.fairlabor.org/projects/covid-19-and-migrant-agriculture-workers-in-the-palm-oil-sector-in-malaysia/).

<sup>51</sup> “Palm oil producers losing up to 25% of potential yield due to labour shortage,” Malaysian Reserve, July 21, 2020, <https://themalaysianreserve.com/2020/07/21/palm-oil-producers-losing-up-to-25-of-potential-yield-due-to-labour-shortage/>.

<sup>52</sup> Varkkey, H., (2016), op. cit.

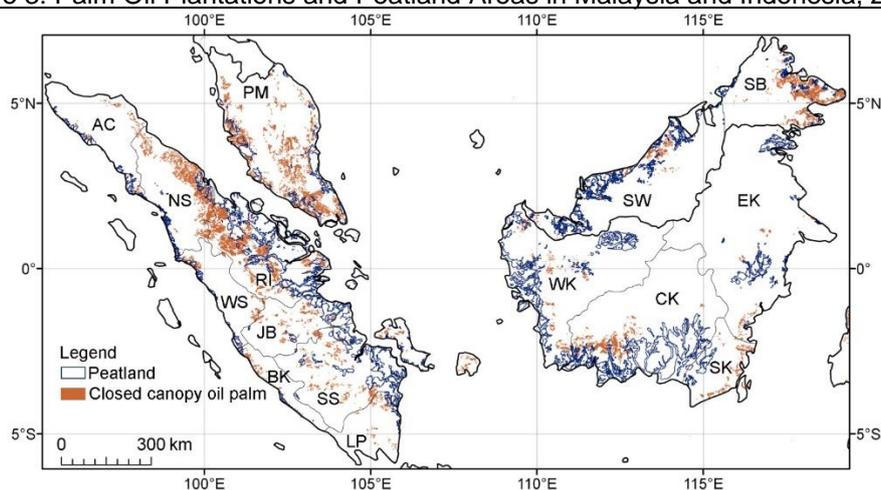
<sup>53</sup> IUCN Oil Palm Task Force, *Palm oil and biodiversity* (IUCN: 2018), <https://doi.org/10.2305/IUCN.CH.2018.11.en>

<sup>54</sup> “8 Things to Know About Palm Oil”, WWF, accessed 2022, [www.wwf.org.uk/updates/8-things-know-about-palm-oil?](http://www.wwf.org.uk/updates/8-things-know-about-palm-oil?)

Demand for palm oil is expected to grow at 1.7% per year until 2050. In response to increasing demand, palm oil production increased 15-fold between 1980 and 2014.<sup>55</sup>

The oil palm thrives in a narrow tropical band about 10 degrees north and south of the equator. However, this equatorial zone is also high in forest cover and biodiversity. Palm oil plantation expansion has been identified as a major driver of deforestation and a grave threat to endangered animals within these areas. In particular, palm oil expansion into peatlands (see Figure 3) has been linked to climate change. In pristine conditions, waterlogged peatlands are excellent carbon sinks. However, when drained for conversion, exposure to air reverses this process and releases large amounts of carbon into the atmosphere. Fires further accelerate this carbon release. Indonesia was listed as among the top three greenhouse gas emitters in 2007, mainly due to carbon release from peatlands.<sup>56</sup> Fire in these peatland areas also contributes to haze. Expansion of plantations into peatlands in both countries either directly or indirectly triggers peat fires which produce toxic smoke that can travel across borders and affect public health and economies across the region.

Figure 3: Palm Oil Plantations and Peatland Areas in Malaysia and Indonesia, 2011<sup>57</sup>



These environmental concerns have soiled the reputation of palm oil regionally and worldwide. Civil society-led movements, mainly in “Western” markets, have culminated in consumer boycotts of items containing palm oil. In 2010, Greenpeace spearheaded a campaign urging consumers to boycott “Killer” Kit Kat and other Nestlé products containing palm oil. In 2018, Greenpeace released an advertisement called “Rang Tan”, highlighting the “25 orangutans we lose every day” to palm oil-linked deforestation.<sup>58</sup> The advertisement was banned in the UK due to “political aims”, and Greenpeace has since shifted its stance away from boycotting palm oil in general towards supporting sustainable palm

<sup>55</sup> IUCN Oil Palm Task Force, (2018), op. cit.

<sup>56</sup> Arga, A., “Indonesia world’s No. 3 greenhouse gas emitter”, Reuters, June 4, 2007, <https://www.reuters.com/article/environment-climate-indonesia-dc-idusjak26206220070604>

<sup>57</sup> Butler, R. A., “First large-scale map of oil palm plantations reveals big environmental toll,” Mongabay, March 7, 2011, <https://news.mongabay.com/2011/03/first-large-scale-map-of-oil-palm-plantations-reveals-big-environmental-toll/>

<sup>58</sup> “Rang-tan: watch the film,” Greenpeace, 2018, [www.greenpeace.org.uk/news/watch-rang-tan-film/](http://www.greenpeace.org.uk/news/watch-rang-tan-film/)

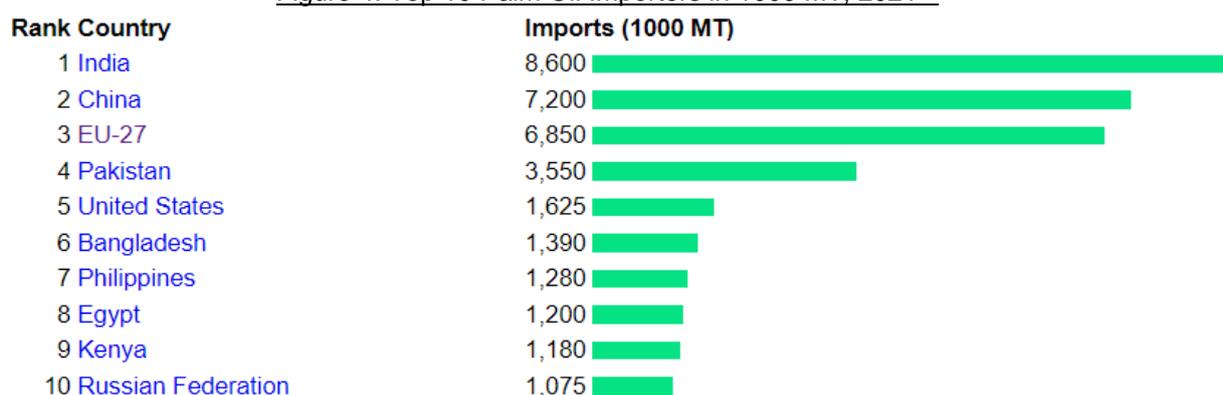
oil. However, consumer sentiment remains, and many products continue to highlight being “palm oil-free” as a unique selling point.

Consumer pressure in Europe spilt into the policy realm when the European Parliament voted in 2018 to phase out palm oil as a feedstock for biofuels by 2021. This culminated in the European Union (EU) Renewable Energy Directive II (RED II) in December 2018, which ruled that high-risk ILUC (indirect land-use change) biofuels should be phased out by 2030. High-risk ILUC biofuels are those produced from a feedstock for which there has been observed a significant expansion of the production area into land with high carbon stock.

While palm oil was not explicitly named, the new requirements for greenhouse gas savings to qualify as low-risk was increased from 35% to 65%. With palm oil clocking in at only 45% of savings, it would be almost automatically disqualified.<sup>59</sup> This would render palm oil “virtually unmarketable” within the EU member states, as palm oil would be more expensive than fossil fuels and domestically produced biofuels without the RED tax benefit.<sup>60</sup> The European Commission is also developing regulations related to deforestation and supply chains which will likely further affect palm oil imports to Europe.

The EU is currently the third-highest importer of palm oil after India and China (see Figure 4). As the external pressures on the palm oil sector translated into actual policy, market access and trade relations would be impacted. This paper posits this as a significant turning point for the issue to be reframed as one of common strategic interests, allowing for conflict and competition to give way to cooperation as both states adopt similar strategic outlooks.

Figure 4: Top 10 Palm Oil Importers in 1000 MT, 2021<sup>61</sup>



<sup>59</sup> Oosterveer, P., “Sustainability of Palm Oil and Its Acceptance in the EU,” *Journal of Oil Palm Research* 32, (September 2020): 365–376, <https://doi.org/10.21894/jopr.2020.0039>.

<sup>60</sup> Meredith, M., “Malaysia’s World Trade Organization Challenge to the European Union’s Renewable Energy Directive: An Economic Analysis,” *Washington International Law Journal* 21, no. 2 (2012): 399.

<sup>61</sup> “Palm Oil Imports by Country in 1000 MT,” IndexMundi, accessed 2021, [www.indexmundi.com/agriculture/?commodity=palm-oil&graph=imports](http://www.indexmundi.com/agriculture/?commodity=palm-oil&graph=imports).

## From Competition to Cooperation

Palm oil policy and governance in both countries have evolved in line with global sustainability pressures. In 2019, Malaysia announced a cap on palm oil cultivated land area at 6.5 million hectares (this currently stands at 5.9 million hectares) by 2023 to keep in line with an earlier pledge made at the 1992 Earth Summit in Rio to maintain 50% of its forest cover. While Indonesia has not committed hard limits to forest use or palm oil expansion, it has declared various moratoriums on deforestation and palm oil. This included the latest Presidential Instruction 5/2019, which turned the temporary moratorium of forest conversion (which is subject to extension every two years) into a permanent rule.<sup>62</sup>

Both countries also introduced their own palm oil sustainability certification system. The Indonesian Sustainable Palm Oil (ISPO) was launched in 2011, while the Malaysian Sustainable Palm Oil (MSPO) was launched in 2014. Commercial players and smallholders must obtain these country-specific certifications to continue their operations in the respective countries. However, ISPO and MSPO are considered generally less stringent than other international certification schemes like the Roundtable for Sustainable Palm Oil (RSPO) and International Sustainability and Carbon Certification (ISCC).

Indonesia and Malaysia also launched public relations campaigns against negative international sentiments. Earlier on, Indonesia had identified these consumer boycotts as “*kampanye hitam*” (black campaigns) by foreign agents to bring down Indonesia’s palm oil industry. In 2019, in a controversial move during the haze season, Indonesia’s Ministry of Communication and Information launched the campaign “*Sawit Baik*” (Good Oil Palm) to raise awareness and combat negative publicity.<sup>63</sup> In 2020, the Malaysian government and the MPOC launched a “*Sawit Anugerah Tuhan*” (Palm Oil – God’s Gift) campaign in 2020 with similar objectives as Indonesia’s campaign.<sup>64</sup>

However, such unilateral efforts have produced lukewarm results. Both countries’ public relations campaigns seem to have backfired as they were dismissed as mere defensive propaganda among Western consumers and governments. This has further tainted perceptions of the sector as a whole, affecting both countries equally and overshadowing the advancements in policy, governance, and certification.

Malaysia, in particular, also faces market pressures outside of Europe related to human rights issues and further politicisation of market access. For example, in 2020, shipments from Sime Darby and FGV were banned from entering the United States due to allegations of labour abuses in their

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<sup>62</sup> Choiruzzad, S. A. B., Tyson, A., and Varkkey, H., (2021), op. cit.

<sup>63</sup> Chadijah, R., “Indonesia Diselar Lancar Kempen Minyak Sawit Meskipun Kebakaran Hutan Merebak,” Berita Benar, September 17, 2017, [www.benarnews.org/malay/berita/my-id-jerebu-190917-09172019161554.html](http://www.benarnews.org/malay/berita/my-id-jerebu-190917-09172019161554.html).

<sup>64</sup> “Ministry launches ‘Sawit Anugerah Tuhan’ campaign,” Bernama, November 19, 2020, [www.bernama.com/en/business/news.php?id=1903003](http://www.bernama.com/en/business/news.php?id=1903003).

operations.<sup>65</sup> In the same year, Malaysian palm oil exports to India were disrupted for four months following a diplomatic spat when (then) Prime Minister Mahathir Mohamed criticised India's revocation of special status to Kashmir and its Citizenship Amendment Act on account of how these developments would affect Muslims there.<sup>66</sup> Exports resumed only after the change of leadership from Mahathir to Muhyiddin Yassin.

The Indian incident illustrated the problems that can arise from periods of political instability. Over the past three years, the Malaysian Prime Ministership has changed three times. Likewise, the Ministership of the Ministry of Primary Industries and Commodities, and related agencies like the Ministry of Environment and Water, and Ministry of Energy and Natural Resources, as well as the leadership of the MPOC, which oversees the MSPO. While there has been no major shift in Malaysia's palm oil sustainability strategy under the current Ismail Sabri administration, it is always more challenging to manage external pressures during periods of internal instability. With Indonesia's comparatively more stable political situation, Indonesia could be a valuable ally providing stability and leadership to both countries' coordinated strategies and responses, at least during this phase of uncertainty.

Furthermore, both countries' increasingly "equal" material capacity in the palm oil sector and the "outsider" pressure towards palm oil sustainability have progressively reframed the issue as one of common strategic interests. Hence, both states are now increasingly reliant on each other's continued prominence for their own market survival, with the recent developments reshaping their conflicting strategic interests in palm oil into complementary strategic outlooks. This is visible through recent multilateral and bilateral cooperative efforts involving both countries.

### ***Multilateral cooperation***

Malaysia and Indonesia jointly founded the Council for Palm Oil Exporting Countries (CPOPC) in 2015 with the broad aim of encouraging mutual cooperation among palm oil-producing countries,<sup>67</sup> and a more specific one of harmonising the MSPO and ISPO schemes.<sup>68</sup> The CPOPC also formed a Scientific Committee in 2021 to focus on research and development activities to "enrich public knowledge on the palm oil commodity".<sup>69</sup>

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<sup>65</sup> "US bans Malaysian palm oil producer over forced labour," BBC, October 1, 2020, <https://www.bbc.com/news/business-54366607>.

<sup>66</sup> "India resumes purchases of Malaysian palm oil: Traders," Economic Times, 2020, <https://economictimes.indiatimes.com/news/economy/foreign-trade/india-resumes-purchases-of-malaysian-palm-oil-traders/articleshow/75821854.cms>.

<sup>67</sup> "Our Mission," CPOPC, accessed 2022, [www.cpopc.org/about-us/our-mission/](http://www.cpopc.org/about-us/our-mission/).

<sup>68</sup> "Malaysia, Indonesia to establish CPOPC," Borneo Post, October 5, 2015, <https://www.theborneopost.com/2015/10/05/malaysia-indonesia-to-establish-cpopc/>.

<sup>69</sup> "Indonesia, Malaysia to bolster cooperation in palm oil industry," Antara News, October 25, 2021, <https://en.antaranews.com/news/195893/indonesia-malaysia-to-bolster-cooperation-in-palm-oil-industry>

While the cooperation over scheme harmonisation did not go far beyond the initial rhetoric, EU RED II served as the landmark impetus for more active collaboration between the two founding members. The CPOPC maintained that the EU's ILUC approach to categorising feedstocks into high ILUC-risk and low ILUC-risk was flawed. Against the backdrop of the Free-Trade Agreement discussions at the 2017 ASEAN-European Union Summit, the CPOPC made a strong statement against the EU RED II, which had been under development at the time.<sup>70</sup> Soon after the RED II was put in place, both countries formed a CPOPC Joint Mission to Brussels in April 2019, which was ultimately unsuccessful in its appeal against the RED II. The CPOPC also filed a formal objection to the EU on the RED II in September 2021.<sup>71</sup>

Both countries also coordinated official requests for consultation with the World Trade Organisation's (WTO) Dispute Settlement Body over "certain measures concerning palm oil and oil palm crop-based biofuels" in relation to the EU RED II.<sup>72</sup> Indonesia submitted its request in December 2019, with a panel being formed in November 2020, and with Malaysia reserving its right to participate in the proceedings as a third party. Malaysia also submitted its own official request for WTO consultation in early 2021. Both countries have argued that the EU RED II violates the WTO's principle of non-discrimination<sup>73</sup> and has the potential to damage the reputation of palm oil in non-biofuel EU markets.<sup>74</sup>

### ***Bilateral cooperation***

Active cooperation over palm oil was a key agenda item during former Malaysian Prime Minister Muhyiddin Yassin's meeting with President Jokowi in February 2021.<sup>75</sup> Looking beyond past grievances related to migrant workers, the Human Resource Ministers on both sides agreed to a pilot project to bring 10,000 Indonesian plantation workers into Malaysia to address labour shortages in the Malaysian palm oil plantation sector as part of both countries' COVID-19 reopening plans in early 2022.<sup>76</sup> Indeed, palm oil continues to dominate the bilateral agenda under the new Malaysian administration. During PM Ismail Sabri's early 2022 meeting with Jokowi in Jakarta, both sides agreed to end the competitive

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<sup>70</sup> Wibowo, R., "Conflict Dynamics Of Protectionism Policy Trading Of Biofuel Commodities Between Indonesia And The European Union," *Proceeding of LPPM UPN "Veteran" Yogyakarta Conference Series 2020 — Political and Social Science Series* 1, no. 1 (2020): 230–237.

<sup>71</sup> "CPOPC Files Objection to EU Targeting Palm Oil in RED II Delegated Act Determining High ILUC-Risk Feedstock," Centre for Sustainable Palm Oil Studies, September 6, 2021, <https://thecspo.org/cpopc-files-objection-to-eu-targeting-palm-oil-in-red-ii-delegated-act-determining-high-iluc-risk-feedstock/>.

<sup>72</sup> "DS593: European Union — Certain measures concerning palm oil and oil palm crop-based biofuels," Dispute Settlement, World Trade Organisation, 2020, [www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds593\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds593_e.htm).

<sup>73</sup> Arief, R. A., Cangara, A. R., Badu, M. N., Baharuddin, A., and Apriliani, A., "The impact of the European Union (EU) renewable energy directive policy on the management of Indonesian palm oil industry," *IOP Conference Series: Earth and Environmental Science* 575 012230, 2020, <https://doi.org/10.1088/1755-1315/575/1/012230>.

<sup>74</sup> Kurniaty, T., "Indonesia Environmental Diplomacy in President Joko Widodo's Era (2014–2019) of the Issue Rejection Indonesia's CPO By European Union," *Sociae Politae* 21, no. 1 (January–June 2020): 74–95.

<sup>75</sup> "Malaysia and Indonesia to co-operate on palm oil trade issue," Economist Intelligence Unit, February 9, 2021, [https://country.eiu.com/article.aspx?articleid=340697817&subtopic\\_3](https://country.eiu.com/article.aspx?articleid=340697817&subtopic_3).

<sup>76</sup> Anis, M. N., "Pilot plan to ease maid shortage," *The Star*, January 25, 2022, [www.thestar.com.my/news/nation/2022/01/25/pilot-plan-to-ease-maid-shortage](http://www.thestar.com.my/news/nation/2022/01/25/pilot-plan-to-ease-maid-shortage).

pricing of palm oil, indicating a move away from the competitive “tariff war” to capture markets based on price.<sup>77</sup>

One of the most obvious shifts in approach has been Malaysia’s diplomatic handling of the transboundary haze issue in 2019. The episode started out closely mirroring past events. The then Malaysian Environment Minister of the new Pakatan Harapan government, Yeo Bee Yin, pointed out that most of the haze experienced by Malaysians came from Indonesia. The Indonesian Environment Minister, Siti Nurbaya Bakar, retaliated with a list of four Malaysian companies in Indonesia sealed off for investigations related to fires.<sup>78</sup>

Following this, however, the Malaysian Minister for Primary Industries and Commodities, Teresa Kok, acted to decompress the situation by stating that it was unfair to keep blaming the palm oil industry on both sides for haze and that such rhetoric was “playing right into the hands of anti-palm oil campaigners”. She also commended the Indonesian government for their improvements in sustainability within the palm oil industry and ground-level haze prevention and mitigation.<sup>79</sup> During the change of government that followed soon after, the new Malaysian Environment Minister of the Perikatan Nasional government, Tuan Ibrahim Tuan Man, shelved the Malaysian Transboundary Haze Act that was due to be tabled at parliament, stating instead that enhanced cooperation with Indonesia would be the preferred strategy.<sup>80</sup>

This episode highlights how transboundary haze, which was traditionally a point of conflict between both countries,<sup>81</sup> has been reframed to protect both countries’ common strategic interests in palm oil. Due to close linkages between palm oil and haze, key government actors in Malaysia have been increasingly willing to overlook transboundary haze issues despite its dire effects on the Malaysian economy and public health. Their goal is to improve the sentiment related to the palm oil sector, not only in Malaysia but also in Indonesia.

## Outlook for the “Special Relationship”

This paper has shown how recent external, policy-level developments that may directly threaten access to markets have encouraged both countries, especially Malaysia, to reframe the palm oil sustainability issue as a common strategic interest. External negative sentiments towards palm oil have tainted perceptions of the sector as a whole, which have affected both countries equally. As a result, both countries have adopted similar strategic outlooks favouring cooperation over competition. Indeed, the

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<sup>77</sup> “Indonesia, Malaysia agree on palm oil non-competition, migrant worker protection,” *The Straits Times*, April 1, 2022, [www.straitstimes.com/asia/se-asia/indonesia-malaysia-agree-their-palm-oil-prices-should-not-compete/](http://www.straitstimes.com/asia/se-asia/indonesia-malaysia-agree-their-palm-oil-prices-should-not-compete/)

<sup>78</sup> Varkkey, H., “No Smoke Without Fire: The Politics of Haze in Southeast Asia,” *Between The Lines*, 2019, <https://betweenthelines.my/no-smoke-without-fire-the-politics-of-haze-in-southeast-asia/>.

<sup>79</sup> Povera, A., “Haze: Kok raises concern over Indonesia’s action against 4 Malaysian companies,” *New Straits Times*, September 13, 2019, [www.nst.com.my/news/nation/2019/09/521216/haze-kok-raises-concern-over-indonesias-action-against-4-malaysian](http://www.nst.com.my/news/nation/2019/09/521216/haze-kok-raises-concern-over-indonesias-action-against-4-malaysian).

<sup>80</sup> Daim, N., “Tabling of Transboundary Haze Act shelved,” *New Straits Times*, August 30, 2020, [www.nst.com.my/news/nation/2020/08/613690/tabling-transboundary-haze-act-shelved](http://www.nst.com.my/news/nation/2020/08/613690/tabling-transboundary-haze-act-shelved).

<sup>81</sup> Clark, M., and Pietsch, J., (2019), op. cit.

combined clout of Malaysia and Indonesia may have contributed to the EU's increased willingness for more constructive engagement over the RED II. The EU agreed to establish a Joint Working Group on Palm Oil Between the European Union and Relevant ASEAN Member Countries for better understanding and possible technical cooperation over sustainability criteria and certification processes. The first meeting of this working group was held in January 2021. However, it remains to be seen how these discussions would pan out.

A special relationship shared between two countries should be a positive thing for both parties. However, the identities that Malaysia and Indonesia hold in common, and their related emotional expectations, have mainly served to amplify the fallout over issues like territorial disputes and illegal immigrants in the past. In contrast, this paper suggests that an increased understanding about *shared* strategic interests in areas such as palm oil can complement the common identities (and vice versa) and positively enhance the “special relationship” between Malaysia and Indonesia. This can also encourage more productive engagement in other traditionally conflictual areas like haze pollution and migrant workers. Hence, for Malaysia and Indonesia to reap more tangible benefits from their “special relationship”, a higher focus on shared strategic interests may be the best way forward.

## About the Author



Dr Helena Varkkey is an Associate Professor at the Department of International and Strategic Studies, University of Malaya in Kuala Lumpur, Malaysia. Her research focuses on the governance of transboundary pollution or “haze” in Southeast Asia. More broadly, she seeks to understand how economic development can be reconciled with environmental sustainability in this resource-rich region. The findings from her PhD at the University of Sydney has been published as a book in 2016 as part of the Routledge Malaysian Studies Series, entitled “*The Haze Problem in Southeast Asia: Palm Oil and Patronage*”. She has consulted for the Ministry of Foreign Affairs, the Academy of Sciences, Malaysia and the ASEAN Secretariat on these topics, and continues to undertake research in this field. She undertook a Visiting Senior Research Fellowship at the Asia Research Institute, National University of Singapore in 2021.

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