

# CHAPTER I

## INTRODUCTION

### A. Background

In the era of globalization, many countries in the world are making International trade. This happens because of two main factors. The first factor is that countries involved in trading activities have different resources with each other. The second factor is that the countries involved in trading activities are equally active in producing certain goods with large quantities and sound quality (Basri & Munandar, 2010).

As we have seen, due to the increase of complex state relations, countries in the world become realize to conduct free trade. The purpose of free trade is to prosper the countries involved in it. Free trade creates a stable and profitable economic order to attract investors to invest in the country and increase trade between countries in the world (Soetrisno, 2002).

In the implementation of free trade, many countries join and establish a Free Trade Area (FTA). One of them is the ASEAN-China Free Trade Area (ACFTA). On July 1996, China became the partner free trade area with ASEAN, and the conference between China and member states of ASEAN which also attended by Japan and South Korea was held in December 1997. China established cooperation based on attitude and trust between both parties (Cheng, December 2001, p. 420).

Indonesia is an ASEAN member country which joins the ASEAN-China Free Trade Area. Since January 1, 2010, Indonesia opens the domestic market freely to the countries of ASEAN and China. The opening of this free market is a concrete manifestation of the implementation of free trade agreements between ASEAN member countries (Indonesia, Thailand, Malaysia, Singapore, Philippines, and Brunei Darussalam) with China, called the ASEAN-CHINA Free Trade Agreement (Cheng, December 2001).

Indonesia is one of the countries that trade interstate bilaterally, regionally, and multilaterally. ACFTA (ASEAN-China Free Trade Area) is one of the cooperation conducted by Indonesia as a member country of ASEAN and China. The purpose of the Indonesian government is to open more extensive domestic and foreign market opportunities and improve the competitiveness products of Indonesia products in ASEAN, China, and world market (Salvatore, 1996).

ACFTA will encourage higher levels of trade in Chinese products to the Indonesian market and bring positive and negative impacts on Indonesia's exports and imports. One of the conditions for a country to be able to benefit from free trade is competitiveness, but studies show some elements the form of competitiveness, such as the level of efficiency, productivity, and business environment in China is relatively better than in Indonesia (Nugroho, 2011, pp. 31-37).

In 2010 this Southeast Asian country incorporated in ASEAN (Association of South East Asian Nation) agreed on China ASEAN Free Trade Agreement or CAFTA / AFCFTA with China. Starting in 2004 ASEAN countries have signed the CAFTA, namely an agreement to start free trade with China with various provisions regarding trade between ASEAN and China such as import duties which are gradually reduced. By the schedule, in 2010 the ACFTA entered the standard track one category on January 1, 2010. ASEAN Connectivity will be held among fellow ASEAN countries, which the Indonesian government anticipates with the operation of the Socah Port in 2020. On the other hand, various parties are concerned that the ACFTA agreement will weaken the national economy, further threatening the termination of employment and leading to an increase in the number of unemployed people in Indonesia due to low competitiveness of Indonesian products, and the unpreparedness of the people to face global competition. In 2010 the Southeast Asian countries incorporated in the ASEAN (Association of South East Asian Nations) agreed on the ASEAN China Free Trade Area or ACFTA with the

Chinese state. Various parties worry that this agreement will weaken the national economy, then threaten trade for domestic industrial products and lead to the rise of layoffs (Lestari, 2014).

Based on data of export growth from Indonesia to China and import growth from China to Indonesia before and after the entry into force of ACFTA can be shown in Table 1.

*Table 1 1.1 Trade Relation Between Indonesia and China 2009-2011 (Thousand US Dollars)*

Year	2009	2010	2011
Export	11,499,327	15,692,611	22,941,005
Import	14,002,171	20,424,218	26,212,187
TradeBalance	-2,502,843	-4,731,607	-3,271,182
Total Trade	25,501,498	36,116,829	49,153,192

*Source: Badan Pusat Statistik, Processed Ministry of Trade*

The Central Bureau of Statistics stated that there was an imbalance in the trade balance between Indonesia and China. The data above shows the value of exports and imports from Indonesia to China. From 2009, the show in the table. The trade balance is calculated at US\$ -2,502,843 from the total trade of US\$ 25,501,498. In 2010, where the application of the ACFTA regime was truly carried out, a trade balance between Indonesia and China was recorded at US\$ -4,731,607 of the total trade of US\$ 36,116,829. Moreover, in 2011 the total trade balance was US\$ -3,271,182 of the total trade of US\$ 49,153,192.

Other data said, in recent years, there was an imbalance in the export-import trade balance between Indonesia and China. The export-import ratio between Indonesia and China shows a deficit figure. Bank Indonesia data (May 2009) stated that in 2006 Indonesia had a deficit of US \$ 0.993 billion. In 2007, the deficit figure reached the US \$ 2.708 billion. In 2008 the figure was the US \$ 7.898 billion. In 2009, the supply of imported goods from China reached the US \$ 12.01 billion, and the deficit figure reached US \$ 4.29

billion (BPS, 2010). In 2010, the trade balance between Indonesia and China experienced a deficit of US \$ 5.32 billion.

Before the entry into force of ACFTA (with tariffs), export growth in Indonesia is smaller than import growth. The condition will affect Indonesia's trade balance which tends deficit, especially after ACFTA (no tariff) is enforced. Indonesia's trade balance is predicted to worsen due to import growth from China. (Firman & Aziza, 2009).

The collective agreement between countries in free trade (without tariffs) has two impacts on global trade and the welfare of its people, the first impact will improve the welfare of its people because free trade can replace high-cost domestic production with low-cost imported goods of the member countries due to the absence of tariffs, the two free trades may also reduce the welfare of the people due to the replacement of low-cost imported goods from non-member countries with similar goods originating from member countries (Kimberly, 2001).

## **B. Research Question**

Based on the background that has been explained above, author identifying the research question is: How Indonesia attempt to rebalance its trade in the face of China's market expansion after the ratification of the ASEAN - China Free Trade Area (ACFTA)?

## **C. Theoretical Framework**

The Theoretical Framework is used to make it easier for the author to answer the hypothesis. The frame of mind used in this study is the theory of free trade.

### **1. Theory of Free Trade**

Free trade is an economic concept that refers to the sale of products between countries without import-export taxes or other trade barriers. With the existence of international cooperation in the field of trade, it can provide an assumption

that it is necessary to cooperate with other countries to develop themselves. Free trade cannot be avoided because countries have interests in it. China in cooperation with ASEAN was concluded indirectly to establish cooperation with ASEAN members.

China cooperates with ASEAN because it indirectly means that China also cooperates with Indonesian countries that are members of ASEAN. The collaboration between Indonesia and China within the framework of ACFTA is a collaboration that is carried out to create free trade. (Wijatno & Gunadi, 2014, p. 194) Defined Free trade is a phenomenon that cannot be avoided. Trade or exchange has a special meaning, namely trade is defined as a process of exchange which is held on the voluntary will of each party. Each party must have the freedom to determine the profit and loss of the exchange from their respective interests and determine whether or not the agreement is made for the exchange.

Trade theory will continue to grow over time. Therefore, the author tries to use endogenous growth theory by Rimer and Lucas (Theory of Endogenous Growth).

The endogenous growth theory states "Decreasing trade barriers in all matters related to anything that inhibits the existence of free trade in the form of tariffs and nontariff, accelerating economic growth and state development in the long run."

Reducing trade barriers will allow developing countries to absorb technology from developed countries. Decreasing these barriers will make relations between countries take place more smoothly. The elimination of barriers will reduce price distortions, another advantage of removing barriers itself is the increase in trade volume which spurs economies of scale in production, thereby increasing profits for entrepreneurs in developing countries.

Free trade is a collaboration between countries or groups of groups of countries that agree to eliminate quotas and regulations. Free trade is the primary foundation of economic development in the ASEAN region and China. The

aim of establishing free trade between ASEAN and China will have implications for the growth of trade in ASEAN countries including Indonesia as a member of ASEAN.

#### **D. Hypothesis**

Based on the formulation of the problem and the theoretical framework above, the author draws the hypothesis as follows: Indonesia attempt to rebalance its trade relation with China through optimizing the opportunity available in the ACFTA as a free trade regime.

#### **E. Research Purpose**

In researching a problem, must have a purpose. The purpose of this study :

##### **1. Objective Purpose**

The study was conducted to explain facts about ACFTA and its impact on Indonesia's economic stability, the effectiveness of preparation and the policy by the government Indonesia to implementing ACFTA, and the study is to analyze The opportunities and challenges of Indonesia in ACFTA cooperation.

##### **2. Subjective Purpose**

To provide exceptional knowledge according to the writer and for the writer himself in the field of research as knowledge gained in college and is expected to provide information for the Faculty of Social and Political Sciences, especially International Relations, and to complete the study of undergraduate (S.1).

#### **F. Research Method**

This research uses descriptive methodology. It is defined by (Nazir, 1988) in the Sample Book of Research Methods, Argued that in terms of the type of problem being investigated, the techniques and tools used, as well as the place and time.

Descriptive method is a method in examining the status of a group of people, an object, a set of conditions, a system of thought or a class of events in the present. The purpose of this descriptive research is to make the description, description, or painting systematically, factually and accurately about the facts, properties and relationships between phenomena investigated (Nazir, 1988, pp. 64-65).

In the detailed methodology used is the descriptive-analytical, In other words, descriptive, analytical research takes the problem or focuses attention to the problem as it is when the research conducted research results are then processed and analyzed to be taken conclusion (Sugiyono, 2009).

This research is using secondary data. The secondary data collection techniques through literature study, the technique of collecting data from bibliography books, information based on a review of literature or references either sourced articles, magazines, newspapers, journals, websites, as well as essential notes on the subject which is related to the problem being investigated by the author. According (Suryani & Hendryadi, 2015).

### **G. Scope of Research**

Because of the extent of the problem in this study, the writer tries to limit the problem by focusing the research on ASEAN-China Free Trade Area, the ACFTA cooperation framework was signed in Phnom Penh, Cambodia, on November 4, 2002, and it was agreed that the establishment of a free trade zone in 2010. On that basis, ACFTA existed on January 1, 2010. Thus ACFTA will be fully implemented after ten years since the signing of the initial agreement (2002-2010).

### **H. Outline**

Overall, the writing of this proposal consists of five chapters. The discussion contained between chapter one and the other chapters is interrelated.

Chapter I: The content of this chapter is the introduction part consisting of the background, research question, theory, hypothesis, research purposes, research method, the range of research, and writing system.

Chapter II: This chapter contains the background of the ASEAN-China Free Trade Area cooperation. The chapter would discuss the meaning of ACFTA, China's relations with ASEAN countries in the context of free trade post-ratification of ACFTA and its implementation.

Chapter III: This chapter consists of development Indonesia – China trade relations, the changing of Indonesia policy, the history Indonesia – China relations, trading relation between Indonesia China before ACFTA implementation, Indonesia government steps face to ACFTA.

Chapter IV: This chapter will implement the impact of ACFTA toward Indonesia's economy, Increase Competitiveness as a Strategy for the Indonesian Government in Facing ACFTA, and Protection from the government in dealing with ACFTA.

Chapter V: Conclusion. Contains conclusions that answer the hypotheses by the author.