

CHAPTER I

Introduction

In the first chapter, this will explain about the background, objectives, problems and writing systematic limitation of this study. This introductory chapter is made to understand overview of this research first before reading this report further.

1.1 Background

China and Indonesia finally became nation state after World War II, but followed different social systems which put strong influence on economic relations between them. Together with the influence of international political regimes in the period of Cold War, the economic relations between China and Indonesia had not been smooth. Economic relations between Indonesia and China are closely related to the political relations between the two countries. As the political relations have been up and down, so have been the economic relations. China and Indonesia established diplomatic relations on 13 April 1950 and signed first bilateral trade agreement in 1953. Afterward, the trade between them had been increased, the total trade value between them increased from US\$ 7.38 million in 1954 to US\$ 129 million in 1959. Even in 1965, China once became the second trade partner of Indonesia which Indonesian import and export value from China occupied 11 percent of the total value of Indonesian import and export.

But following the '30 September' incident in 1965, Indonesia's second president, Suharto, officially came to power in a 1965 counter coup against communist and sympathetic military elements. Jakarta's growing political

alignment with Beijing under first president, Soekarno, had culminated in the months prior to the coup attempt in Indonesia's withdrawal from the United Nations and the announcement of a political axis between Indonesia and China. Awash with rumors that Beijing was arming the PKI (Partai Komunis Indonesia, Indonesian Communist Party) political tensions in Indonesia exploded violently and spectacularly following 30 September 1965. The anti-communist credentials of Suharto's New Order regime became an important source of its domestic political legitimacy and an excuse for repression of dissent and denial of ethnic Chinese their basic rights.

This had a significant negative impact on the economic relations between Indonesia and China. Until 1980s, Relations between China and Indonesia began to ease. In July 1985, the Indonesian Chamber of Commerce and the China Council for the Promotion of International Trade (CCPIT) signed a memorandum of understanding (MoU) for the reestablishment of a direct trade link between the two countries. Five years later, it was on 8 August 1990 while Premier Li Peng was visiting Indonesia, the Chinese and Indonesian foreign ministers signed the Memorandum of Understanding on Restoration of Diplomatic Relations on behalf of each of his own government. After that, the political and economic relations between the two countries had been normalized, The relation shave seen all-round progress and developed rapidly. Average annual growth rate of trade reached 14.7 percent during 1990-2000.

Entering 21st century after the Cold War was ended; the relations between the two countries have been in best time. In May 2000, Foreign Minister Tang

Jiaxuan and Indonesian Foreign Minister Alwi Shihab signed in Beijing the Joint statement on the Course for Future Bilateral Cooperation between the People's Republic of China and the Republic of Indonesia, and Memorandum of Understanding on the Joint Committee of Bilateral Cooperation between the People's Republic of China and Republic of Indonesia, which was the guideline of developing the relations between two countries in 21st century. This showed that the two countries reached consensus on establishing and developing all-round cooperative relations based on long-term stability, mutual trust and good neighborliness.

Cooperation between Indonesia and China had just established will bring Indonesia into a better direction. The relations between Indonesia and China tend to be the best way to compromise the Indonesia economic interest such as trading. Imagine if we live without trading system. We have to grow our own rice, grains, fruits, and vegetables that we consume. We also have to grow things that even its hard grows in the territory; we have to find things that cannot be found in the territory. Life gets better when working together, when we have trading system. With trading we can specialized, and also would find the variety of product.

Trading could happen not just in the inter-regional but also can happen internationally. The Inter-regional trade and specialization has resulted in increased efficiency in production and consumption. But with the sovereignty of the state, interstate commerce is not as free as before. Many obstacles in selling goods to other countries, or vice versa. Barriers can occur from the seller or from the buyer. These constraints make the cost of traded goods more expensive.

Therefore, the absence or reduction of costs (barriers) is expected to increase trade and prosperity in all the countries involved in this trade. That is the basic assumption of the necessity created a free trade agreement (free trade agreement / FTA).

The heads of agreement for the Indonesia-China FTA, which forms part of the wider ASEAN-China FTA (ACFTA) - was signed in late 2004. And it just held on January 1, 2010, ASEAN and China has implemented FTAs. ASEAN countries are referred to: Indonesia, Malaysia, Singapore, Brunei, Vietnam, the Philippines, Cambodia, Laos, Thailand and Myanmar.

ACFTA is a form of collective cooperation, it aims to strengthen and enhance economic cooperation, trade and investment between member states. It progressively liberalizes and promotes trade in goods and services and creating a system that is transparent and to facilitate investment. And also facilitate the more effective economic integration of the new ASEAN members (Cambodia, Laos, Myanmar, and Vietnam-CLMV) and bridging the gap economic development among member countries.

Each of the ASEAN member and China has a tremendous potential in trade, ASEAN has a large and attractive market; China on the other hand has also been developed a worldwide market. This corporation will bring the huge market, and tremendous changes in Asian market.

Sees from Indonesia interest perspective, there are opportunities that Indonesia has with joining the multilateral economic agreement such as ACFTA such as increased market access for exports to China with a lower tariff rate for

national products. Increased access to services in the China market for service providers nationwide also increased foreign investment flows from China to Indonesia. The opening of the transfer of technology between businesses in the two countries.

The agreement of ACFTA is the result of import duty china manufacturing products to ASEAN, Indonesia referred to, set a maximum of 5%, and 0% in the agricultural sector without any taxes at all. ACFTA is the embodiment of the concept of interdependence between countries, especially ASEAN member countries and China. This is manifested in terms of economic interdependence, in which each country specializes in producing each particular commodity so it will be more efficient for those countries where export and import trade.

In addition, the geographic market opportunities and their bond is also a major factor interdependence of ASEAN countries and China. China sees huge market opportunity of the ASEAN member countries, ASEAN countries (including Indonesia) also saw a huge market opportunity in China and could providing significant potential for increasing trade and investment exchange between China and Indonesia.

Economic relations between Indonesia and China improved along with the new millennium. China in particular, was able to become one of Indonesia's largest trading partners. According to data released by the Central Statistics Agency (BPS), between 2003 and 2004, or the period after the implementation of the initial stage of the ACFTA, in January 2004, and not long after that,

Indonesia's exports to China increased by 232, 20 per cent, while imports from China increased by only 38.67 percent.¹

Indonesia saw a rapid economic rise of China as an opportunity for cooperation between the two sides. Under the government of President Susilo Bambang Yudhoyono, the Indonesian government enters the latest phase in the cooperation with the Chinese government. Strategic partnership has made a positive impact for both parties. Indonesia and China relations gained momentum with the signing of the *Joint Declaration between the Republic of Indonesia and the People's Republic of China on Strategic Partnership* by the two heads of state on 25 April 2005 in Jakarta.²

ACFTA also one of the reason Indonesia strengthen the bilateral economic cooperation to China which is focused at increasing cooperation in investment, infrastructure, agricultural, forestry and energy sectors, including the development of small and medium enterprises.

The corporation between Indonesia and China not free from challenges and obstacles. Number of policy changes that have been made by China, making the integration of China in Asia region, a strong integration, which competes with commodities from ASEAN countries. To that end, this integration has led to a strong challenge for Indonesia as a member of ASEAN.

¹<http://15yrfhdyt.wordpress.com/2012/02/13/perkembangan-kerjasama-bilateral-ekonomi-indonesia-dan-china-dari-tahun-1967-2006-dalam-lingkup-pengaruh-acfta-di-kawasan-asean/>. Accessed on 24 September 2011

² <http://indonesianembassy-china.org/>. Accessed on 24 September 2011

Bilateral cooperation between Indonesia and China is a diplomatic relationship that is idealistic and competitive. Many things that benefit from this cooperation, will create a dynamic bilateral relations, along with the competitive Chinese products are spreads over the market of Indonesia, Indonesia should be able to balance the distribution of income distributing products from China, which has occupied the top-level market distribution system. Yet behind the economic competition, in both countries, namely Indonesia and China, the two countries is so much build up diplomacy in other areas, in addition to economic, Indonesia and China are involved in the G-20 (The Group of Twenty Finance Ministers and Central Bank Governors), and included in the ASEAN plus 3, and trade Organization WTO. This proves that Indonesia and China still have an ongoing relationship in terms of political cooperation, which is where the relationship is necessary to support each other in an effort to increase the intensity of the support of the international trust.

Of course there are a lot of propaganda about free trade Indonesia China, but Indonesia should have a benchmark in what Indonesia will do in maintaining economic interests, so there will be no a huge imbalance caused by the ACFTA. FTAs have become an element of Indonesia's international economic diplomacy. Indonesia will negotiate FTAs only with a few major trading partners, and the policy is to aim at producing high quality agreements. This is a big challenge and can be overcome through systematic efforts to build capacity and to clearly formulate the strategy to actively engage in bilateral, regional, and multilateral trade agreements.

There are various areas of cooperation that is covered in the ACFTA, in which areas of cooperation include cooperation in investment area as well as trade in goods and services. The debate among the various levels of society occur because of the thought on the challenges and opportunities for Indonesia in the ACFTA. Opportunities for Indonesia in ACFTA is that the inclusion of China's market access in and removal of trade barriers, economic efficiency, comparative advantage, increasing national income, economic growth, meeting the domestic demand, rising foreign investment, and increasing bargaining power with China in Indonesia in facing Indonesia's uncertain economy circumstances. The challenge for Indonesia is also not a few, namely, the existence of market liberalization in ACFTA, this suggests that Indonesia should be able to improve the efficiency and effectiveness of production in order to be more competitive in the face of the world market. Lack of foreign investment (FDI) in Indonesia due to infrastructure and rule of law in the country that is less clear and transparent is also one part of the challenge for Indonesia.

Government prepared several tactical steps as anticipation to protect national industry that was indicated crisis caused by the implementation of ASEAN-China free trade agreement. Based on the industrial ministry's data, the industry that was indicated crisis consisted of textile, footwear, electronics, furniture on wood and rattan, children toys, machinery, iron steel, food and beverages, as well as cosmetics.

Meanwhile through the bilateral and diplomatic effort, China government promised to change the economic pattern in the next 5 year by multiplies import of products from Indonesia, than previously dominated by exports to Indonesia and countries in ASEAN. The Vice Minister of Publicity Department of Communist Party of China (CPC) Central Committee Shen Wei Chen said in the China Publicity Congress, government had issued the 12th middle term plan of 5 year by creating significant change in the economic field. There were significant changes in the pattern of economic such as China will increase import from Indonesia in order to fulfill the domestic need (compared to exporting its products).³

Besides that, there are two aspects that very important. First is influence of political economy, if a country does not have the economic strength, then a country will not be taken into account at all. Even if there is a huge population in, but still, weak economy would not be at all taken into account. For example in the ASEAN region, based on economy condition, the influential one is Singapore, Singapore considered a small country, but Singapore has been taken into account due to its great economic power.

The second aspect, is trade. For Indonesia, the trade is one means of communication with China, in a larger sense is that, Indonesia offset the uncertainty and also uses the trade network, namely, to compensate for changes in

³ Source : Bisnis Indonesia, Monday, April,11, 2011. Page. 1. Accessed on 19 September 2012

economic uncertainty within the ASEAN region. So does China, it wants to improve its previous bad image in the eyes of Southeast Asia.

China would affect the strength of this country in global politics, Furthermore, Indonesia also affect the strength of regional politics in relation of ACFTA, only if Indonesia could take benefit in facilitating the country to play a leadership role in Southeast Asia. To achieve that, Indonesia should have the readiness and strength in the economy. Therefore, by using trade context is a means to strengthen the economy of Indonesia and plays a leadership role in the area of Southeast Asia, especially ASEAN.

Based on the background above, this analysis will review “ **THE IMPLEMENTATION OF ACFTA: CHALLENGES AND OPPORTUNITIES FOR INDONESIA PERIODE 2010-2012**”

1.2 Research Question

- i. What are the Opportunities and Challenges that Indonesia has to face in relations with ACFTA?
- ii. Does the bilateral relationship Indonesia-China will strengthen Indonesia in ACFTA?

1.3 Purpose

- To know the opportunities and challenges for Indonesia related to ACFTA.

- To identify the effect of bilateral relationship Indonesia-China regard to ACFTA.

1.3 Problem Limitation

In order for this study did not deviate from the purpose and have maximum results it needs to be some restrictions on the problem. This paper only describe about:

1. Historical background such as the relationship between Indonesia and China.
2. China Economic Rise
3. Rational ACFTA
4. Trade Relations and Agreements in ACFTA 2004-2012
5. The challenges and opportunities that Indonesia has to face regarding to ACFTA.
6. Bilateral trade relations between Indonesia and China in ACFTA
7. Results of bilateral relations between Indonesia and China

1.4 Research Plan

Research Plan part of writing is one of the most crucial in the writing of scientific papers. This section contains an explanation of the order and report writing. By reading the research plan of writing, the reader is expected to be able to understand the sequence of writing the chapters, the contents, and the relation between the chapters in this report. This report consists of five chapters where

each chapter has several sub-chapters. Here is a description of the research plan of this report:

CHAPTER I INTRODUCTION

This chapter will explain about background, research question, purpose of the thesis, and the research plan.

CHAPTER II CONCEPTUAL FRAMEWORK

This chapter contains the theories derived from relevant sources and used in conducting and completing the study.

Theories relating to the collection and processing of data.

CHAPTER III RESEARCH METHOD

Chapter describes the research methods on the measures taken in this study. The research method gives a detailed explanation of the research done and the sequence diagram and the research process. By reading this chapter the research method, the reader is expected to be easier to get an understanding of the research process.

CHAPTER IV DATA ANALYSIS

This chapter suggests common data and special needs to achieve the objectives of this study. In this chapter will analyze the study about:

4.1 China Economic Rise in Interdependence Era

4.2 ASEAN-Free Trade Area.

4.3 Rational Establishment of ACFTA

4.4 Opportunities and Challenges for Indonesia in ACFTA

**4.5 Bilateral trade relations between Indonesia and China in
ACFTA**

**4.6 Results of bilateral relations between Indonesia and
China**

CHAPTER V

CONCLUSION AND RECOMMENDATIONS

This chapter is the last chapter in this research report. This chapter written about the conclusions of this study, it also displays the advice given and suggestions are expected to be.



