

Indonesia – China Trade Relations: The deepening of economic integration amid uncertainty?

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Abstract

This paper examines the way in which Indonesia responded to the full implementation of the ASEAN–China Free Trade Agreement (ACFTA) in early 2010. More specifically, it looks at the domestic negotiation processes that took place between the Indonesian government and its stakeholders, and between the governments of Indonesia and China. As part of its policy recommendations, the paper proposes that Indonesia, other ASEAN member countries and China should address the potentially negative implications of the ACFTA and identify ways in which this trade agreement could assist the acceleration of domestic economic reforms in all participating countries.

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Abbreviations and Acronyms

ACFTA	ASEAN–China Free Trade Agreement
ASEAN	Association of Southeast Asian Nations
EHP	Early Harvest Program
EPA	economic partnership agreement
FTA	free trade agreement

Executive Summary

The full implementation of the Association of Southeast Asian Nations (ASEAN)–China Free Trade Agreement (ACFTA) in early 2010 caused much anxiety in Indonesia. The country’s private sector and civil society organizations insisted that the government either pull Indonesia out of the agreement or renegotiate its terms with Beijing. Reluctant to breach an international trade agreement, which would harm the country’s rising international stature in recent years, the government instead agreed to renegotiate up to 228 tariff lines with its Chinese counterpart.

Notwithstanding such a compromise, skepticism about ACFTA implementation remains strong in the country, which has a long tradition of protectionism. Even prior to the implementation of this trade agreement, the Indonesian market, as was the case with other ASEAN members, was already flooded with cheap, often illegal, imports from China. Skeptics also blamed the Indonesian government for failing to inform the public properly about the signing and subsequent implementation of the ACFTA, and added that the recent initiatives to address the negative impacts of this trade agreement were a case of too little too late.

There is little doubt that China will feature strongly in Indonesia’s trade relations with the outside world for quite some time to come. Given the limited space now available for Indonesia to either pull out fully from or renegotiate this trade agreement, it is now necessary for both sides to concentrate on the realization of the ACFTA’s potential economic benefits as promised under the 2002 Framework Agreement on Comprehensive Economic Cooperation between ASEAN and China.

For example, Indonesia, other ASEAN member countries and China could identify ways in which the ACFTA could assist domestic economic reforms in all of the participating countries. This was, after all, the basic premise on which most of ASEAN’s and/or Indonesia’s other free trade deals were based. Moreover, the ACFTA could also be improved by providing an extended agreement for both sides to set up social safety-net programs that enable the participating countries to address the negative impacts of the ACFTA’s implementation. Apart from that, both sides could also consider exploiting and expanding further the coverage of the so-called “Other Areas of Economic Cooperation” within the above-mentioned Framework Agreement to include cooperation in the areas that might be affected by trade liberalization, including, but not limited to, the environment.

1. Introduction

The full implementation of the Association of Southeast Asian Nations (ASEAN)–China Free Trade Agreement (ACFTA) in early 2010 caused much anxiety in Indonesia. The country’s private sector and civil society organizations vigorously lobbied the Indonesian government and members of parliament, insisting that Indonesia should either pull out of the agreement or renegotiate its terms with Beijing. It was, naturally, a difficult demand for the Indonesian government to meet. Reluctant to breach an international trade agreement, which would harm the country’s rising international profile in recent years, the Indonesian government also realized that meeting either one of these demands made little sense, since at the time of the debates the country was already in the middle of ACFTA implementation. Indeed, little known to the public, the early phase of this free trade agreement, known as the Early Harvest Program (EHP), had actually been implemented since 2004. As a compromise with its domestic constituents, the Indonesian government agreed to renegotiate up to 228 tariff lines (Kabar Bisnis, 2010) and proposed the establishment of a working committee to oversee and tackle the negative effects that the ACFTA may generate in Indonesia (Ekawati, 2010).

Notwithstanding such a compromise, skepticism about the benefits of ACFTA implementation remains strong among pressure groups in Indonesia. Even prior to the implementation of this free trade agreement, the Indonesian market had been flooded by cheap, often illegal, imports from China (Pambudi & Chandra, 2006). Some domestic observers blamed the Indonesian government for failing to inform the public properly about the signing and subsequent implementation of the ACFTA¹ and further argued that more recent initiatives to address the negative impacts of this trade agreement, including the above-mentioned renegotiation of the 228 tariff lines and the establishment of a working committee on the issue, were a case of too little too late. Who is to blame for this was a matter of perspective. While the government bears its share of the responsibility for executing the negotiations and striking a deal with ASEAN member countries and China, the public too, particularly civil society groups, should accept some responsibility for failing to pressure the negotiating parties to create a fully mutually beneficial free trade agreement when negotiations began in the early 2000s. It was only in mid-2009, a few months away from full ACFTA implementation, that influential business groups and civil society organizations began voicing their concerns about this free trade deal.

There is little doubt that China will feature strongly in Indonesia’s trade relations with the outside world for some time to come. Given the limited space now available as a result of political, geostrategic and other practical considerations for Indonesia to either pull out fully from or renegotiate the trade agreement, it is now necessary for both sides to concentrate on the realization of the potential economic benefits of the ACFTA as promised under the 2002 Framework Agreement on Comprehensive Economic Cooperation between ASEAN and China. For example, those involved in the agreement could identify ways in which the ACFTA could assist domestic economic reforms in participating countries. This was, after all, the basic premise on which most of ASEAN’s and/or Indonesia’s free trade deals were based (i.e., the argument that free trade helps promote domestic economic reforms). While the earlier phase of full ACFTA implementation has concentrated on the trade in goods, most of which would have relatively little effect on the already highly liberalized Indonesian and ASEAN manufacturing sector, this free trade agreement could be improved by providing an extended agreement for both sides to set up social safety net programs that enable participating countries to address the negative impacts of the ACFTA’s implementation. Furthermore, both sides could also consider exploiting and further expanding the coverage of the so-called “Other Areas of Economic Cooperation” within the above-mentioned Framework Agreement to include cooperation in the areas that might be affected by trade liberalization, including, but not limited to, the environment.

1 See, for example, Susanto (2010).

This paper therefore argues that, despite the overwhelming attention given to the competitive effect of Chinese products vis-à-vis Indonesia's (Zain, 2011), the latter should not lose sight of the longer-term strategic objectives of this trade agreement. Firstly, in light of China's growing importance as the world's second-largest economy and the largest in Asia, it will be very difficult for Jakarta to ignore Beijing. Secondly, embracing China is also strategic, as it allows both Indonesia and ASEAN as a whole to better manage their relations with other major powers. At the same time, however, although renegotiation of the terms of the ACFTA is not only difficult, but might also take a long time, the voices of domestic pressure groups matter. In its effort to attain developed-country status, although China has made a lot of mistakes, it also seems willing to learn from them. Therefore, the key question is how Indonesia and ASEAN are able to exploit Beijing's willingness to adjust its position so as to enable fully mutual economic benefits for all involved.

2. Patterns of Trade Relations between Indonesia and China

Table 1: Total trade between Indonesia and China, 2006–2010 (USD billion)

	2006	2007	2008	2009	2010	Trend (%)
Total trade	14.9	18.2	26.8	25.5	36.1	23.31
Oil and gas	4.0	3.6	4.1	3.0	2.3	-11.55
Non-oil and gas	10.9	14.6	22.7	22.4	33.7	30.68
Exports	8.3	9.6	11.6	11.4	15.6	15.44
Oil and gas	2.8	3.0	3.8	2.5	1.6	-12.31
Non-oil and gas	5.4	6.6	7.7	8.9	14.0	24.41
Imports	6.6	8.5	15.2	14.0	20.4	31.53
Oil and gas	1.1	6.0	0.299	0.510	0.736	-9.77
Non-oil and gas	5.5	7.9	14.9	13.4	19.6	36.04
Indonesia's trade balance with China	1.7	1.1	-3.6	-2.5	-4.7	0.00
Oil and gas	1.7	2.4	3.5	2.0	0.875	-14.18
Non-oil and gas	-0.01	-1.2	-7.1	-4.5	-5.6	-0.00

Source: Ministry of Trade of the Republic of Indonesia (n.d.a)

Since the full implementation of the ACFTA in January 2010, trade between Indonesia and China has been on the rise. Total trade between the two sides had, in fact, risen significantly since ASEAN and China agreed on the implementation of the EHP, which took effect in early 2005. Indeed, while in 2003 trade between Indonesia and China reached only USD 3.8 billion, the total trade figure rose to USD 14.9 billion in 2006. Between 2006 and the end of 2009 trade between Indonesia and China increased by USDD 10.5 billion. Although prior to EHP implementation total trade between the two countries favoured Indonesia, since 2006 the gap between the country's exports and imports vis-à-vis China had narrowed. Indeed, while in 2006 Indonesia experienced a trade surplus of USD 1.7 billion with China, this figure was reduced to USD 1.1 billion in the following year. By 2008 total trade between the two countries began to shift in favour of China, which had a USD 3.6 billion trade surplus with Indonesia. This figure was USD 2.5 billion in 2009 (refer to Table 1).

Furthermore, China has also been one of Indonesia's key major trading partners in recent years, serving as the country's largest export and import market. In terms of total non-oil and gas exports, China stood as the third-largest destination for Indonesian export products in 2006 behind Japan and the United States, a trend that lasted until the end of 2009. By 2010, however, China had managed to overtake the United States as Indonesia's second-largest trading partner. Indeed, Indonesia's non-oil and gas exports

to China more than doubled in the period 2006–2010. While in 2006 Indonesia’s non-oil and gas exports to China stood at USD 5.4 billion, in 2010 this figure reached USD 14.0 billion. Moreover, in terms of the overall trend of non-oil and gas trade, Indonesia’s exports to China have also showed a most promising outlook, rising by about 24.4 per cent, in contrast to Japan and the United States, exports to which increased by only 5.28 per cent and 3.72 per cent, respectively (refer to Table 2). Similarly, China is also becoming Indonesia’s most important source of imports. For example, non-oil and gas imports from China rose from USD 5.5 billion in 2006 to USD 19.6 billion in 2010. During the same period, the overall trend of non-oil and gas imports from China to Indonesia also showed a significant increase of around 36.04 per cent, which is higher in comparison to other major sources of Indonesian imports, including Japan (30.56 per cent) and the United States (23.42 per cent) (refer to Table 3).

Table 2: Indonesia’s major export destinations, 2006–2010 (USD billion)

Rank	Country	2006	2007	2008	2009	2010	Trend (%)
1.	Japan	12.1	13.0	13.7	11.9	16.4	5.28
2.	China	5.4	6.6	7.7	8.9	14.0	24.41
3.	United States	10.6	11.3	12.5	10.4	13.3	3.72
4.	India	3.3	4.8	7.0	7.3	9.8	29.44
5.	Singapore	7.8	8.9	10.1	7.9	9.5	2.80

Source: Ministry of Trade of the Republic of Indonesia (n.d.b)

From China’s perspective, since 2010 ASEAN as a whole has become its fourth-largest trading partner after the European Union, Japan and the United States. Among ASEAN member countries, Indonesia was China’s fourth-largest trading partner, which, according to data as of May 2010 from the Ministry of Commerce of the People’s Republic of China, amounted to USD 12.4 billion, after Malaysia (USD 22.2 billion), Singapore (USD 17.9 billion) and Thailand (USD 15.7 billion). Between May 2009 and May 2010 the Department of Asian Affairs of the Ministry of Commerce of the People’s Republic of China also noted that, despite a trade deficit of USD 5.95 billion, China saw a 57.7 per cent increase in the value of its exports to Indonesia and a 92.1 per cent increase in the value of its imports from that country.

Table 3: Major sources of Indonesian imports, 2006–2010 (USD billion)

Rank	Country	2006	2007	2008	2009	2010	Trend (%)
1.	China	5.5	7.9	14.9	13.4	19.6	36.04
2.	Japan	5.4	6.4	14.8	9.8	16.9	30.56
3.	Singapore	3.7	3.9	11.0	9.2	10.0	32.86
4.	United States	3.9	4.7	7.7	7.0	9.2	23.43
5.	Thailand	2.9	4.1	6.2	4.5	7.4	21.20

Source: Ministry of Trade of the Republic of Indonesia (n.d.c)

Despite growing trade between Indonesia and China, Indonesia is increasingly under pressure in this area. Indeed, as of May 2011, the Indonesian Central Statistics Agency announced that the country’s trade surplus slid to USD 1.81 billion, in comparison to USD 2.4 billion in the preceding February and USD 1.91 billion in January (*Jakarta Post*, 2011). The decrease in Indonesia’s trade surplus was mainly due to the widening of its trade deficit with China. Whereas in February 2011 Indonesia’s trade deficit with China reached USD 1.34 billion, the figure went up slightly to USD 1.37 billion in the following month. Although other factors, such as the appreciation of the Indonesian rupiah against the dollar, have contributed to a sharp increase in imports, Indonesia’s increasing trade deficit with China has been the Indonesian media’s main focus of attention.

Table 4: China's trade relations with ASEAN countries, 2010 (USD billion)

	Trade value	Trade increase/ decrease (%)	Balance of trade
Brunei	0.36	517.4	-0.234
Cambodia	0.38	33.6	0.345
Indonesia	12.4	74.0	-0.595
Lao PDR	0.42	73.3	-0.019
Malaysia	22.2	68.4	-7.690
Myanmar	1.319	76.8	0.798
Philippines	8.25	49.5	-1.264
Singapore	17.9	42.2	3.418
Thailand	15.78	60.4	-4.786
Vietnam	7.926	50.1	4.168
ASEAN	86.575	104.57	-5.859

Source: Ministry of Commerce of the People's Republic of China (2010)

Table 5: Indonesia's export/import data as of March 2011 (USD billion)

	Feb. 2011	March 2011	Jan.–March 2010	Jan.–March 2011	Monthly change (%)	Yearly change (%)	Contribution (%)
Total imports	11.75	14.48	29.96	38.79	23.23	29.46	100
Consumption	0.91	1.29	2.18	3.23	41.87	48.19	8.32
Raw materials	8.72	10.53	21.84	28.67	20.7	31.32	73.93
Capital goods	2.12	2.66	5.95	6.89	25.63	15.77	17.75
Oil and gas	2.54	2.88	6.23	8.39	13.06	34.63	21.64
Non-oil and gas	9.21	11.6	23.73	30.39	26.04	28.1	78.36
Total exports	14.42	16.29	35.54	45.31	13.03	27.51	100
Oil and gas	2.61	2.97	6.69	8.2	13.64	22.54	18.09
Non-oil and gas	11.8	13.32	28.85	37.12	12.88	28/66	81.91

Source: *Jakarta Post* (2011)

3. Why an ACFTA?

3.1 ASEAN and China as Natural Economic Partners

Despite the perceived and real problems that it generates, the ACFTA is still considered the major pillar of the new era of ASEAN–China economic relations. It was in fact one of the earliest of the so-called bilateral free trade agreements or comprehensive economic partnership/cooperation agreements that ASEAN undertook with its dialogue partners in the early 2000s. The engagement with ASEAN was important for China, since it served as the diplomatic stepping stone to the latter's engagement with the wider global community. Likewise, once considered as a hostile foe by most, if not all, ASEAN member countries, China's ability to embrace the ASEAN bloc through this trade agreement also signified Beijing's intention to use economic statecraft as a way to improve its position peacefully among the major global powers (Wang, 2005).

Indeed, at the time, ASEAN featured greatly in China's overall foreign security and economic policy direction. Apart from sharing long borders with some ASEAN member countries, ASEAN's relative success as a regional grouping among developing countries played a considerable role in influencing policy-makers in Beijing to embrace their southern neighbours.² Southeast Asia's relatively large market and the richness of its natural resources were assets that could help fuel China's economic growth. More importantly, however, precisely because of ASEAN's relative attractiveness vis-à-vis other major powers, each of which had its own strategic political and economic rationales to engage with ASEAN, Beijing saw a closer relationship with ASEAN as an imperative. China used its growing economic prowess to have a greater say in regional political-security and economic architectures, and was keen to balance the influences of other major powers, particularly the United States, in its own backyard.

As far as Indonesia was concerned, policy-makers in Jakarta saw China's economic opening, particularly following its accession to the World Trade Organization in 2001, and its intention to engage ASEAN as a whole as both an economic opportunity and a threat. It was an opportunity because China's 1.2 billion people were a huge potential market for Indonesian exporters to exploit. This rationale was also supported by the significant growth of the country's trade with China since the normalization of diplomatic relations in the early 1990s. From 1993 to 2003, or prior to the implementation of the EHP, trade between the two sides increased by 32 per cent, or from USD 1,249.4 billion to USD 3,802.5 billion (Pambudi & Chandra, 2006). Pambudi and Chandra (2006) also report that between 2003 and 2004 alone Indonesia's exports to China rose by as much as 232.20 per cent, while its imports from China rose by a mere 38.67 per cent. The favourable trend in the trade between Indonesia and China made a sufficiently convincing argument for Indonesian policy-makers to engage in ACFTA negotiations.

At the same time, however, China's potential economic engagement with Southeast Asia was also seen as a threat by Jakarta. Throughout the 1990s until the early 2000s, for example, the economies of both China and Indonesia did not complement each other in that they produced, exported and imported similar products in the global market. This was apparent in terms of several Indonesian manufactured products, such as textiles and garments, and footwear. Although this was to change following the greater diversification of Chinese exports to Southeast Asian economies in the mid-2000s, this too presented a host of new challenges to the Indonesian economy, which in turn undermined the bilateral relationship between the two countries. As with other Southeast Asian countries involved in the ACFTA deal, the Indonesian economy was flooded with cheap Chinese imports, which caused some uproar in the country. For example, the Indonesian Chamber of Commerce and Industry (Kamar Dagang dan Industri Indonesia) has for the last few years been voicing its concern over the difficulties faced by local industries in coping with the massive flood of Chinese imports (Rima News, 2011). Other influential private sector groups, such as the Indonesian Textile Association (Asosiasi Pertekstilan Indonesia) also claimed that textile imports from China controlled up to 50 per cent of the local market in West Sumatra (Haluan, 2011). Despite this, advocates of free trade, including those in policy-making circles, argued that the long-term benefits of the ACFTA for the national economy would outweigh the costs, and would contribute to economic growth and welfare (Zain, 2011).

² Some Chinese scholars, such as Wang Jiang Yu (2005), even admit to China's concern over being left out by ASEAN regional integration schemes and not being included as a major trading partner of the grouping.

3.2 ASEAN and China and the Quest for Free Trade Agreements/Economic Partnership Agreements

Free trade agreements (FTAs) and/or economic partnership agreements (EPAs), whether in their multi-lateral, regional or bilateral forms, are becoming one of the critical components of foreign diplomacy in the East Asian region. Indeed, according to Kawai and Wignaraja (2010), by June 2010, 45 FTAs had been adopted in the region over the previous decade as a means to pursue country-level and regional trade strategies. These authors also add that the large economies of Northeast Asia, including China, Japan and South Korea, are taking the lead in forging FTAs/EPAs with their trading partners. As with its counterparts in Northeast Asia, ASEAN and its member countries are also no strangers to FTAs/EPAs. While ASEAN as a whole has concluded FTAs/EPAs with six major trading and/or strategic partners, including China, Japan, South Korea, Australia, New Zealand and India, individual member countries of the grouping are pursuing similar forms of economic diplomacy with more diverse trade partners. Among other things, the overall shift from a neo-mercantilist to a neo-liberal approach to trade policy (Dent, 2002), the passion for deepening regional economic integration and the difficulty of concluding the World Trade Organization's Doha Development Round of negotiations (Chandra, 2005) have been some of the key rationales for the emergence of these FTA/EPA initiatives.

As for China specifically, Beijing has become more confident in the international trade arena following its accession to the World Trade Organization in 2001, which took the country more than 15 years of exhaustive negotiations with the then-150 member countries of this world trade body. Not long after its accession, China embarked on bilateral and/or regional trade agreements with the surrounding countries and/or territories that were its primary free trade partners, such as Hong Kong, Macao, ASEAN, Australia and New Zealand. By 2009 China had managed to conclude bilateral FTAs with Hong Kong, Macau, ASEAN, Chile, New Zealand, Pakistan, Singapore and Peru, as well as being a party to the Asia-Pacific Trade Agreement (PWC, 2009).³ For China, its strategy of concluding FTAs enables it to ensure market access for its exports, expand outward investment and solidify its position as the regional hub of an advanced production network (Kawai & Wignaraja, 2010).

While there has been strong consensus among Chinese policy-makers and domestic constituents about the potential benefits of the country's FTA strategy, the same cannot be said in Southeast Asia. Indeed, different countries in the region deal with the emergence of the FTA/EPA phenomenon differently. While more-open economies in Southeast Asia, such as Singapore, Malaysia and Thailand, have spear-headed the establishment of bilateral and regional FTAs/EPAs, others have been relatively slow in responding to this trend. Indonesia in particular was very late in pursuing bilateral FTA/EPA negotiations with its major trading partners in comparison to the three ASEAN member countries mentioned above. Indeed, although the early phase of an FTA with China was already in place in 2004, it was only then that the Indonesian government finally decided to consolidate its free trade strategy (Chandra, 2005). At the time, the then-Indonesian coordinating economic minister, Dorodjatun Kuntjorojakti, said that the increasing number of bilateral FTAs/EPAs concluded by the country's major trading partners was

³ Initially known as the Bangkok Agreement, the Asia-Pacific Trade Agreement, which was originally signed in 1976, was renamed on November 2005. It is the oldest preferential trade agreement among the developing countries of the Asia-Pacific and aims to promote regional trade through the exchange of mutually agreed concessions by member countries. Since it was initiated by the UN Economic and Social Commission for Asia and the Pacific, membership is also open to all developing members of this UN body. To date, membership includes Bangladesh, China, India, South Korea, Laos and Sri Lanka (UNESCAP, 2007).

likely to have discriminatory effects on Indonesian products in these markets (Bisnis Indonesia, 2004). In other words, the fear of being left out prompted Indonesian policy-makers to pursue active engagement on bilateral FTAs/EPAs. In light of strong public pressure for Indonesia to reconsider its position in the free trade deal with China in early 2010, however, the government decided to postpone new FTA/EPA negotiations (Antara, 2010a) and instead focus on existing free trade deals.

4. ACFTA Implementation and Its Implications for Indonesia

4.1 Policy Regime under ACFTA Implementation

ACFTA implementation was undertaken gradually in all participating countries. China was particularly aware of perceptions of the “China threat” among Southeast Asian countries. Precisely because of this, China agreed, firstly, to pursue the implementation of this trade deal step by step, with special and differential treatment given to the least-developed members of ASEAN, and, secondly, allowed the EHP to be installed in the early phase of the agreement. In principle, the EHP allowed ASEAN member countries to export a list of their agricultural products to China without their being subjected to tariffs. Overall, 530 products were listed under the ASEAN–China EHP (HS 10 digit), excluding sweet corn and fruits, with 47 agricultural products listed under the Indonesia–China EHP (HS 20 digit), which included coffee, coconut oil, fat, margarine, cacao, soap, rattan products and stearic acid (Pambudi & Chandra, 2006).

In Indonesia, the implementation of the early phase of the ACFTA was ratified by Presidential Decree No. 48/2004 on the Endorsement of the Framework Agreement on Comprehensive Economic Cooperation between ASEAN and China.⁴ Subsequently, the minister of finance issued two related decrees: Finance Ministerial Decrees No. 355/KMK.01/2004 on the Provision of Import Tariffs under the EHP and No. 356/KMK.01/2004 on Tariff Provisions under the EHP-ACFTA (both were issued on 21 July 2004). The former in particular laid down the rules of origin regulations and the imposition of a maximum of 5 per cent tariff rate for the previously mentioned 530 tariff lines. The reduction of tariffs on products listed under the EHP began on 21 July 2005. In 2005 Finance Ministerial Decree No. 57/PMK.010/2005, which set the tariff rates under the ACFTA’s normal track program, was also issued. In total, there were 263 tariff lines (six digits) under this track. As for the tariffs on sensitive and highly sensitive products, these are to be phased out gradually between 2012 and 2018.⁵

4.2 Implementing the ACFTA in Indonesia: Public Sentiments vs. Actual Impacts

Public opinion was strongly divided over ACFTA implementation in Indonesia. While little attention was given to the process of ACFTA negotiations that took place between 2001 and 2003, public interest in the subject increased following concerns expressed by the private sector and government ministries dealing with economic matters over the possible negative impacts of the ACFTA for Indonesia. In July 2009 the private sector, spearheaded by major associations such as the Indonesian Chambers of Commerce and Industry and the Association of Indonesian Entrepreneurs (Asosiasi Pengusaha Indonesia), launched public advocacy activities to pressurize the government to reconsider its position on this trade

⁴ In Indonesia, the ACFTA was ratified under the administration of President Megawati Soekarnoputri.

⁵ As with the normal track program, tariffs under the sensitive and highly sensitive tracks will be phased out on a gradual basis. Tariff reduction under the sensitive track program commences in 2012, when all tariffs should reach a maximum 20 per cent. This is then to be further reduced to 0 per cent by 2018. By 2015 all tariffs under the highly sensitive track will have to be reduced by a maximum of 50 per cent. Products listed under the sensitive track include finished leather products, bags, footwear, spectacles, musical instruments, toys, sporting goods, stationery, steel, antibiotics, and glass and plastic goods, whereas those under the highly sensitive track include agricultural products (rice, sugar, corn and soya), textiles, and automotive and ceramic tableware products.

agreement. On behalf of the industries it represented, the Indonesian Chambers of Commerce and Industry made a public statement that when fully implemented, the ACFTA was likely to be harmful to industries (KADIN, 2010). Shortly afterwards, in August 2009 the Ministry of Industry, through an internal study carried out on the ACFTA, added a similar warning against this free trade deal (Chandra, 2010). By the end of 2009 a meeting between the Ministry of Industry, which was then headed by M. S. Hidayat, a former head of the Indonesian Chambers of Commerce and Industry during the period 2004–2009, and representatives of the private sector was organized. On that occasion, no less than 14 industries expressed their reservations about complying with ACFTA commitments.⁶ It was at this time that these industries came up with the idea of renegotiating the terms of the ACFTA agreement and submitted a list of 309 tariff lines, which was later brought down to 228 in early 2010, whose tariff reduction commitments should be delayed until a new time frame was agreed with Beijing (Republika, 2009).

Complementing this opposition to the ACFTA were the mass demonstrations that took place in several main cities in early 2010. On 20 January 2010, for instance, Western Javanese farmers who were members of the Indonesian Farmers' Council (Dewan Tani Indonesia) and the Opposition People's Front (Front Rakyat Oposisi) organized a mass rally against the ACFTA throughout the main areas of Bandung, West Java's capital. Shortly thereafter, on 27 January 2010, over 20 labour associations made a statement rejecting the ACFTA agreement at a press conference (Hukum Online, 2010). This was then followed by occasional mass demonstrations by various labour groups in the capital and other main cities throughout the year. Moreover, learning from previous successes using social network sites such as Facebook, Indonesian civil society groups also launched aggressive public campaigns to undermine the country's commitment to the ACFTA. To date, at least two main public campaigns have appeared on Facebook, i.e., the "5 Million Movement against the ACFTA" (Gerakan 5 Juta Tolak ACFTA) and the "Civil Society Coalition against the ACFTA" (Koalisi Masyarakat Sipil Tolak ACFTA), which managed to gather 1,196 and a mere 168 supporters, respectively.⁷

The general sentiment against the ACFTA was best illustrated by a survey of the Indonesian public's perceptions of this trade agreement carried out by the Indonesian Survey Institute (Lembaga Survei Indonesia) in May 2010.⁸ Conducted through face-to-face interviews with up to 1,000 respondents, the survey revealed interesting, although not very surprising, results. For example, it revealed that only 26.7 per cent of the public had actually heard of the ACFTA, and among those that were aware of the agreement, 51.9 per cent expressed reservations about it. Up to 55.1 per cent of these latter interviewees also said that they feared the potential flooding of Indonesia by cheap Chinese imports, which would damage the country's economy in the long term. Meanwhile, 21 per cent of those who supported the agreement said that the ACFTA could benefit Indonesian exports to China. While this survey illustrates the general sentiments that have emerged in Indonesia about the ACFTA, it should also be read with caution, as the media, often backed by certain business and political interests, play a significant role in influencing public opinion.

6 The 14 industries included tires, furniture, glass sheeting, cacao-processing, vehicles, petrochemicals, health equipment, cosmetics, aluminum products, footwear, appliance equipment, textiles, steel and electronics.

7 For the "5 Million Movement against the ACFTA" Facebook account, see www.facebook.com/group.php?gid=246488869393&v=wall; for the "Civil Society Coalition against the ACFTA" Facebook account, see www.facebook.com/group.php?gid=122907537719856.

8 For further details of this survey, see LSI (2010).

Ironically, the euphoria about the ACFTA also jeopardized the unity of the so-called United Indonesia Cabinet II, the name given to the current Indonesian cabinet under the administration of President Susilo Bambang Yudhoyono that attempts to reflect the unity of the diverse political and professional backgrounds of its members. Although under pressure from its domestic constituents to reconsider the country's position vis-à-vis the ACFTA, some members of the cabinet and their respective ministries remained adamant that Indonesia should fully commit to ACFTA implementation. As a genuine supporter of trade liberalization, the minister of trade, Dr. Mari E. Pangestu, and the country's other ministers dealing with economic matters (the coordinating minister for economic affairs, the minister of small and medium-sized enterprises, the minister of state owned-enterprises and, to a certain extent, the minister of finance) have on several occasions played down the threat presented by the ACFTA. On one occasion, for instance, Pangestu stated that, apart from the need to pay China large compensation as part of the renegotiation package, the government has taken the steps necessary to anticipate the negative impacts of the ACFTA (Antara, 2010b).⁹ Notwithstanding growing concern about the trade deal, Pangestu finally submitted a formal letter to the ASEAN secretary general, Dr. Surin Pitsuwan, on December 2009 highlighting the difficulties that Indonesia may face from the implementation of this trade agreement. The letter, however, failed to mention Indonesia's intention to renegotiate ACFTA implementation. Not only did this incident spark resentment towards the minister among the protectionist business groups, but it also created friction between the trade and industry ministries, the latter of which is well known for its protectionist proclivity. At the height of the debate in early 2010 the minister of industry even stated that the success of the negotiation would depend on the lead negotiator, which is the trade minister. However, unconvinced by Pangestu's willingness to renegotiate the ACFTA, the minister of industry also added that "I'd be ready to take the role [as the lead negotiator] if asked" (Antara, 2010c).

As a response to the public's anxiety about the ACFTA, the parliament or People's Consultative Assembly (Dewan Perwakilan Rakyat), led by Commission VI, which oversees trade, industry, investment, cooperative, small and medium-sized enterprises and state-owned enterprises affairs, summoned five ministers dealing with economic affairs (including the trade, industry, finance, state-owned enterprises, and small and medium-sized enterprises ministers) to provide clarification about the progress of ACFTA renegotiation. Upset with the seemingly half-hearted effort by the minister of trade to make the renegotiation process a reality, the members of Commission VI put Pangestu on the spot. In her defense, she reasoned that ACFTA renegotiation would also require the willingness of other ASEAN member countries to renegotiate with China. Despite this, the members of the commission insisted that the renegotiation initiative should go ahead. Shortly after the meeting, the commission also decided to set up a working committee (Panitia Kerja) not only to oversee the renegotiation process (should it ever take place), but also to prepare domestic industries to manage ACFTA implementation (Baren, 2010).

Jakarta finally had the chance to present its argument for ACFTA renegotiation during the 10th Indonesia–China Joint Commission Meeting at Yogyakarta on 3 April 2010. Speaking at a press conference after the meeting, the Chinese trade minister, Chen Deming, stated that it was imperative for both sides to apply the ACFTA as scheduled in order to keep their two-way trade balanced, sustainable and profitable (Antara, 2010d). The minister also added that China would assist the competitiveness of Indonesia's small and medium-sized enterprises through programs for equipment renewal, investment promotion and trade facilitation. On top of this, China also pledged up to USD 2 billion to finance infrastructure development in Indonesia as part of the ACFTA deal with the country. While the meeting was seen as a failure by the private sector, Pangestu, on the other hand, considered it as having accommodated the interests of Indonesian entrepreneurs. She stated her government's intention to solve

⁹ It was for this reason that Pangestu opted instead for organizing special bilateral talks with China that can be used as a forum to discuss more comprehensive trade issues, rather than as a specific forum for the renegotiation of the terms of the ACFTA.

the problems related to tariff reduction of the 228 tariff lines through a comprehensive government program aimed at improving industrial competitiveness (Jakarta Post, 2010). Another key agreement reached at the Yogyakarta meeting was for the establishment of a joint working group or expert group committee to overcome the potential negative impacts of ACFTA implementation. Both Indonesia and China, however, missed the deadline for the establishment of this group by June 2010. There is also lack of clarity on how effective the group's work has been.¹⁰

As expected, the supposed failure of the Indonesian negotiating team to renegotiate the terms of the ACFTA irritated many in the country. Shortly after the Yogyakarta meeting, the minister of industry, M. S. Hidayat, expressed his disappointment with the result of the renegotiation and claimed that Pangestu, the lead negotiator, was solely responsible for Indonesia's decision to proceed with the ACFTA. He also blamed the Ministry of Trade for having failed to consult effectively with other ministries dealing with economic affairs on the substance of the negotiations (Wulan, 2010). The head of Commission VI, Airlangga Hartato, also criticized the trade minister and contended that the outcome of the Yogyakarta meeting would upset the business sector (Suara Pembaruan, 2010). Representing the view of the business sector, meanwhile, the secretary general of the Association of Indonesian Entrepreneurs, Franky Sibarani, warned of potential losses of up to USD 1.2 billion due to the failure of the Indonesian government to renegotiate the 228 tariff lines. He also added that of this amount, only USD 43 million would be compensated for by the infrastructure development aid program offered by China to Indonesia (Media Indonesia, 2010). Overall, despite China's promised economic compensation package, a pessimistic view remained of Indonesia's capacity to cope with ACFTA implementation.

Indonesia's ACFTA policy, naturally, was strongly defended by the country's policy-makers. In a seminar on the Prospects for Indonesia–China Relations: Empowerment for National Interests organized by the Sinar Harapan daily in November 2010, for example, a number of high-ranking officials argued that the ACFTA still generates substantial benefits for Indonesia (Antara, 2010e). At the time, the deputy minister for economic affairs responsible for industry and trade affairs, Edy Putra Irawadi, insisted that since the implementation of the EHP in early 2005, trade between Indonesia and China had risen by about 22.26 per cent, or from USD 12.5 billion in 2005 to USD 25.5 billion in 2009. Irawadi further stipulated that, based on data from the Indonesian Investment Coordinating Board (Badan Koordinasi Penanaman Modal), Chinese investment in Indonesia had expanded to cover infrastructure development and the natural resources sector. During the same event, the deputy trade minister, Mahendra Siregar, also added that during President Yudhoyono's visit to Shanghai in October 2010, the private sectors of the two countries agreed to sign 27 memoranda of understanding, which included USD 5 billion worth of Chinese investment in Indonesia covering oil and gas, agribusiness, fisheries, and the mining sector, as well as infrastructure development. All these were seen by Indonesian officials as positive trends that had emerged from the deepening of economic relations between the two countries.

A number of Indonesian economists and international trade experts have also supported Indonesia's continued engagement in the ACFTA. A scholar from the Atma Jaya Catholic University, Dr. A. Prasetyantoko (2011), for instance, argued that the rise of imports from China can be seen positively, particularly if they serve as a source of support for the revitalization of Indonesian domestic industry. In February 2011 alone, as he further explained, the value of non-oil and gas imports was dominated by machinery and mechanical equipment, rising up to 18.87 per cent from the previous year, which is a positive sign of the relative increase of complementarity between the Chinese and Indonesian economies. Even at the provincial level, an economist from the University of North Sumatra, Jhon Tafbu Ritonga, also argued in a public lecture about the North Sumatran economy in early 2011 that, judging from the trade balance

¹⁰ As stated by an anonymous representative of the Indonesian Chambers of Commerce and Industry on 5 May 2011.

between North Sumatra and China, the province still has the capacity to gain benefits from the ACFTA. In fact, in comparison to the national trade balance vis-à-vis China, which only increased by 23.71 per cent over the previous year, the trade balance between China and North Sumatra rose by 109.74 per cent during the same period. North Sumatra was able to exploit the benefits offered by the ACFTA because the province possessed various commodities needed by China, including crude palm oil and rubber (Harian Medan Bisnis, 2011).

Furthermore, commenting on Indonesia's possible retreat from or delay in implementing the ACFTA, the director of the Institute for Economic and Social Research (Lembaga Penyelidikan Ekonomi dan Masyarakat), Dr. Arianto Patunru, contended that the private sector's resistance shortly prior to the implementation of this trade agreement was disappointing. Apart from the fact that the agreement had already been in place since 2004, backing off from the ACFTA was not an option for Indonesia, as this would significantly impact the country's credibility as a trading partner (Perspektif Baru, 2010). He also added that in principle, FTAs, including the ACFTA, should encourage the establishment of a more efficient and competitive economic environment. The strong resistance from Indonesian economic actors towards this trade agreement was possibly an illustration of how ineffective the country's private sector was. Another economist, Dr. Anggito Abimanyu of the University of Gadjah Mada and the former head of the Fiscal Policy Department at the Ministry of Finance, also stated that renegotiation with China was not needed, as this would entail a long process and high costs that could be counterproductive for Indonesia as a whole. Renegotiating a single tariff line would require Indonesia to come up with a convincing argument to convince both China and the other ASEAN member countries of the actual negative impacts of the current terms of the agreement that would affect the industry concerned (Wasiyati, 2011).

In early 2010, at the onset of the debate about the ACFTA's potential impacts on Indonesia, one of the authors of this paper also presented a strong argument as to why the demand of several state and non-state actors either to pull out from or delay the implementation of the ACFTA was unreasonable (Chandra, 2010). Firstly, the framework agreement for this free trade deal had already been signed in 2004. At the time, not only had Indonesia and the other ASEAN members been given a period of six years to prepare for full implementation, but the Chinese had also offered the EHP scheme to give ASEAN members early benefits from the trade deal, but this had been underutilized in Indonesia. Secondly, the move either to pull out from or delay the implementation of the ACFTA would also give bad signal to the international community that would be harmful to Indonesia's rising international standing. Thirdly, because of the tendency of the government's overall economic policy to adopt market mechanisms, excessive protectionist attitudes and policies would undermine the economic reforms that had been achieved in the country. Given the past protectionist tradition in Indonesia, it would be very unlikely that businesses and politicians would both be satisfied with the terms of the ACFTA even if implementation of the agreement were to be delayed by five, ten or even 15 years.

5. Conclusion: The Deepening of Economic Integration amid Uncertainty between Indonesia and China

Through the ACFTA, Indonesia and ASEAN are currently in the process of integrating their economies with China. The process of economic integration between the two sides, however, is not without its problems. Ever since the early phase of the ACFTA, i.e., the EHP, was put in place in 2005, economic problems relating to the surge of imports or the rise in the price of commodities were reported in many parts of Southeast Asia. The cool reaction of the Indonesian private sector and civil society organizations towards the establishment of the ACFTA back in 2004 was surprising, particularly given the size of the country's economy and the potential advantages that this agreement could generate for the Indonesian population as a whole. To a large extent, Indonesia was slow in responding to this FTA. While debates about the need for renegotiation will continue for quite some time, there is a need for Indonesia to realize that, in light of the country's growing economic interdependence and integration with the global economy, substantial domestic economic reforms are needed. In comparison to other free trade initiatives that Indonesia and ASEAN are pursuing or will pursue in the future, the ACFTA can be considered as one of the simplest, in that it focuses more on trade in goods, although this can be expanded with the agreement of both parties.

As emphasized in the opening section of this paper, despite the overwhelming attention given to the negative impacts of the ACFTA, Indonesia should not lose sight of the longer-term strategic objectives of this trade agreement. There is little doubt that, given China's emergence as a major economic power, Beijing will feature significantly in Indonesia's trade relations with the world. In its efforts to become a major economic power, although China may make a lot of mistakes, it also seems willing to learn from them. The key question for Indonesia, therefore, is how the country should exploit Beijing's willingness to adjust its position in regard to the negative impacts of the ACFTA.

Overall, the ACFTA could serve as a lesson learned for Indonesia. Firstly, in light of the country's greater economic integration with the world economy, free trade agreements will matter greatly for Indonesia. The pursuit of a free trade strategy should, therefore, be dealt with more cautiously, because such agreements will entail significant impacts on and adjustments for the population of the country as a whole of both a positive and negative kind. Secondly, because of the potential significant impacts that an FTA could generate for the country's economy, consultation with all stakeholders is essential. In relation to the consultation issue, policy-makers should also realize that free trade policies do not only concern the private sector, but also the wider consumer group as a whole, and, as such, consultations with wider stakeholders beyond the private sector are needed. Thirdly, despite their understanding of the importance of Indonesia's engagement with the world economy, the majority of Indonesian policy-makers and politicians, for various political reasons, remain half-hearted about trade liberalization. Socialization about the government's trade liberalization policy is needed not only to enhance greater government transparency, but also to increase public awareness of the potential gains and costs of the government's free trade policies. Fourthly, although this has never been heard of in any international trade agreement thus far, a specific clause covering the formation of a system of social safety nets could be included in any future FTAs that Indonesia might negotiate.

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