



Journal of Current Southeast Asian Affairs

Booth, Anne (2011), China's Economic Relations with Indonesia: Threats and Opportunities, in: *Journal of Current Southeast Asian Affairs*, 30, 2, 141-160.
ISSN: 1868-4882 (online), ISSN: 1868-1034 (print)

The online version of this article can be found at:
<www.CurrentSoutheastAsianAffairs.org>

Published by
GIGA German Institute of Global and Area Studies, Institute of Asian Studies and
Hamburg University Press.

The *Journal of Current Southeast Asian Affairs* is an Open Access publication.
It may be read, copied and distributed free of charge according to the conditions of the
Creative Commons Attribution-No Derivative Works 3.0 License.

To subscribe to the print edition: <ias@giga-hamburg.de>
For an e-mail alert please register at: <www.CurrentSoutheastAsianAffairs.org>

The *Journal of Current Southeast Asian Affairs* is part of the GIGA Journal Family which
includes: Africa Spectrum ● Journal of Current Chinese Affairs ● Journal of Current
Southeast Asian Affairs ● Journal of Politics in Latin America ●
<www.giga-journal-family.org>

China's Economic Relations with Indonesia: Threats and Opportunities

Anne Booth

Abstract: The paper examines the development of China's economic ties with Southeast Asia over the last two decades, culminating in the inauguration of the ASEAN-China Free Trade Agreement (ACFTA) in 2010. Particular reference is made to China's trade ties with Indonesia. Although two-way trade between China and Indonesia has grown rapidly since 2000, Indonesian exports to China are dominated by primary products, while imports from China are dominated by manufactures. While this pattern might reflect short-term comparative advantage in both economies, it is causing some concern in Indonesia. The paper assesses these concerns, and possible political reactions.

■ Manuscript received 25 May 2011; accepted 3 October 2011

Keywords: China, ASEAN, FTA, economy

Prof. Dr. Anne Booth is a Professor of Economics with reference to Asia, School of Oriental and African Studies (SOAS), University of London, UK. Her research interests include long term trends in the economic development of South East Asia.

E-mail: <ab10@soas.ac.uk>

Introduction

This paper examines the evolution of economic relations between China and Southeast Asia over the past two decades, with particular reference to the case of Indonesia. The paper tries to set out both the benefits and costs of increasing trade and investment ties with China for the ASEAN countries and in the case of Indonesia it explores the extent to which competition from China can be blamed for the country's economic problems since the crisis of 1997/98. The paper also examines the ASEAN-China FTA (ACFTA) and analyses the fears which have been expressed in the media, both in Indonesia and in other parts of ASEAN, about free trade with China. Are these simply expressions of economic nationalism on the part of special interest groups, or do these fears have economic validity? Particular attention is paid to whether the rise of China is forcing several ASEAN countries back to what could be termed a "colonial pattern of trade" whereby they produce raw materials in exchange for manufactured imports. If this is in fact the case, especially for Indonesia, what are the longer term consequences for Indonesia's economic development in the medium term? Before discussing this question, the paper gives some background on evolving China-ASEAN economic interactions.

The Background: China and Southeast Asia

During the second half of the 20th century, Chinese economic ties with Southeast Asia attracted little attention, either from academics or from business and the media. After the Chinese Communist Party took control of the mainland in 1949, China's trade and investment ties with most of non-communist Asia declined compared with pre-1942 figures. Migration flows, which had been significant until the 1930s, very largely stopped. The Chinese populations in Southeast Asia, many of whom had been residents in countries such as Thailand, Malaysia, Singapore, and Indonesia for several generations, were not for the most part particularly sympathetic to the Chinese Communist Party, and most had little desire to return to the land of their ancestors. They preferred to accommodate themselves to the independent governments which took control in the decade after 1945; if they left they usually went to Singapore, Hong Kong or Taiwan, to the old colonial metropolises, or to the USA, Canada and Australia. Those who did return to China often had a troubled time over the 1960s. Even after China began to open up to the outside world in the early 1980s, trade and investment ties with Southeast Asia were small.

China's accelerated economic growth through the 1980s and into the 1990s led to some growth in trade and investment flows with Southeast Asia, but these were minor compared with the growth in Southeast Asia's trade and investment flows with Japan, Korea and Taiwan, the USA and Western Europe. In addition, trade and investment flows within Southeast Asia grew after 1980. In 1990, when ASEAN (Association of Southeast Asian Nations) membership still only comprised six nations, per capita GDP in all six was higher than in China (Table 1). By the mid-1990s, four of these six countries had achieved over three decades of sustained economic growth, and were selected for inclusion in the World Bank's 1993 "Asian Miracle" report (Singapore, Malaysia, Thailand, and Indonesia). The World Bank, and many other observers, argued that these countries had "got their policies right" and should be taken as models by less successful economies in other parts of the developing world. The 1993 report, written in the aftermath of the violence in Tiananmen Square, did not include China as one of the Asian miracles, although there was some discussion of the "growth spillover" from Hong Kong into southern China.

Table 1: Per Capita GDP, 1990 and 2007: ASEAN Countries and China (USD; 2005 prices)

	1990	2007
China	1,924	7,868
ASEAN-6		
Brunei	53,391	50,569
Singapore	21,648	44,599
Malaysia	8,449	17,893
Thailand	5,451	9,407
Philippines	3,397	4,791
Indonesia	3,236	5,186
ASEAN-3		
Vietnam	1,473	3,743
Cambodia	1,268	2,824
Laos	1,244	2,280

Note: The figures refer to per capita GDP in 2005 prices, (Laspeyres index, derived from growth rates of consumption, investment and government expenditures).

Source: Penn World Tables version 6.3 <http://pwt.econ.upenn.edu/php_site/pwt63>.

Even in the latter part of 1996, when influential commentators were already pointing to signs of trouble in some of the miracle economies, especially in Thailand, few expected that the economies in Southeast Asia would be in any way "threatened" by China. The financial crisis which hit much of the region in the latter part of 1997 and the ensuing capital outflow triggered a

growth collapse in 1998 in several countries, and a slow economic recovery, especially in Thailand and Indonesia. In 2001, there was a further growth slowdown, especially in Malaysia and Singapore, as a result of falling world demand for electronics exports. By contrast, the Chinese economy was, or appeared to be, booming. By the early 2000s, a number of studies were emerging which suggested that China's membership of the WTO would pose a considerable threat to other exporters, both in Asia and in other parts of the world. In the Asian context, there were several strands to this argument but the main two were that Chinese exports of labour-intensive manufactures (textiles, garments, footwear, toys, low-end electronics) would out-compete those of other Asian economies in the major OECD markets. In addition, as a result of its abundant supplies of cheap labour, huge investments in infrastructure and improvements in the legal and regulatory environment, foreign investment would flood into China at the expense of other parts of developing Asia. As per capita GDP in China grew, and a large middle class emerged, it was argued that more foreign investment would be oriented to the domestic market rather than to export production. But in either case, investment flows to the ASEAN countries would be affected.

By the early years of the 21st century, there seemed to be plenty of evidence to support these fears. Let us examine the evidence on investment first. The share of the main Southeast Asian economies in total capital inflows into ASEAN plus China and Hong Kong contracted sharply after 1998, and had not recovered by 2004 (Ravenhill 2006: 656). Net foreign investment flows in several ASEAN economies, particularly Indonesia, fell in absolute terms after 1997 and recovery was erratic. After 2002, inflows of foreign direct investment into the ASEAN economies did begin to grow again, especially in Singapore and Thailand (Athukorala and Wagle 2011: Figure 4). But with the onset of the global financial crisis in 2008, there were fall in ASEAN as a whole (Table 2). Furthermore, several ASEAN countries had, by the early 21st century, begun to export capital to other parts of the global economy. UNCTAD data showed that in 2007, capital outflows from ASEAN were around fifty billion dollars, although they fell in 2008 and 2009 (Table 2).

Table 2: FDI Inflows and Outflows, 2007-2009 (USD billion)

Region	2007	2008	2009
Inflows			
World	2,100.0	1,770.9	1,114.2
Developed Economies	1,444.1	1,018.3	565.9
Japan	22.6	24.4	11.9
USA	265.9	324.6	129.9

Region	2007	2008	2009
Developing Economies	564.9	630.0	478.4
China	83.5	108.3	95.0
Hong Kong	54.3	59.6	48.5
ASEAN	74.0	47.3	36.8
Indonesia	6.9	9.3	4.9
Outflows			
World	2,267.6	1,928.8	1,101.0
Developed Economies	1,923.9	1,571.9	820.7
Japan	73.6	128.0	74.7
USA	393.5	330.5	248.1
Developing Economies	292.2	296.3	229.2
China	22.5	52.2	48.0
Hong Kong	61.1	50.6	52.3
ASEAN	50.2	15.4	21.3
Indonesia	4.7	5.9	3.0

Source: UNCTAD 2010: Annex Table 1.

On the commodity trade side, a number of studies using computable general equilibrium models or other quantitative techniques showed that China would continue to take market share in a number of labour-intensive products from other developing countries, including those in ASEAN (Tongzon 2005: 194). Unsurprisingly, Tongzon found that the product categories where Chinese competition would be most fierce were textiles and garments, footwear and some electrical products. In common with other analysts, Tongzon pointed out that the main source of China's competitive advantage were low unit labour costs; he also stressed that China's large and rapidly growing domestic market allowed firms to achieve economies of scale which further lowered costs, compared with other developing countries. Another study showed that the ASEAN-4 (Indonesia, Thailand, Malaysia, and the Philippines) all experienced drops in manufactured exports relative to the pre-crisis trends (Woo 2006: 79). Certainly the rapidly growing China market presented opportunities for exports from ASEAN into China. But Tongzon (2005: 209) also pointed out that, even after its entry into the WTO, there remained a range of non-tariff barriers in China including inefficient customs administration and weak enforcement of rules and regulations governing imports at the regional level.

Given the considerable diversity within ASEAN by the early 21st century, it was hardly surprising that different countries viewed the "threats and opportunities" offered by China's growing trading might in different ways. In Singapore, Malaysia and Thailand, where per capita GDP is higher than China, and where the manufacturing sectors are more linked into the "Factory Asia" production networks, China's rise has created greater trading

opportunities. In the Malaysian case a recent study has found that FDI inflows have been positively correlated with those into China which suggests complementarity rather than competition in FDI-led industrial development between the two countries (Athukorala and Wagle 2011: 126). The poorest ASEAN economies such as Laos, Cambodia and Myanmar, have benefited from both Chinese trade and investment, although as other papers in this issue point out, the increasing influence of China has brought problems to these countries as well. In the three “intermediate economies”, Indonesia, the Philippines and Vietnam, there can be no doubt that Chinese competition has led to problems for exporters of labour-intensive manufacturers. But in all three economies trade and investment links with China have grown over the last decade. The next section looks at the Indonesian case in more detail.

The Indonesian Growth Slow-down and Recovery: Causes and Consequences

When world oil prices began to fall in Indonesia in the early 1980s, the Suharto government embarked on a series of reform measures which were designed to make the non-oil export sector more competitive, including two large devaluations, a duty drawback scheme for exporters, and measures to make ports more efficient. By the early 1990s these reforms seemed to have been very successful; the manufacturing sector grew rapidly, and exports of textiles, garments, footwear and wood products all increased. But the growth collapse which followed the Asian crisis in 1997/98 was extremely severe in Indonesia, and recovery was slow. Per capita GDP only regained its 1997 level in 2004. The cost of recapitalizing a devastated banking sector was enormous, and most of the burden fell on the government budget.¹ This meant much needed government investment in education and infrastructure had to be drastically cut back. Government infrastructure investment had already slowed in the final years of the Suharto regime, when powerful private firms, often controlled by the presidential extended family and their cronies were given lucrative contracts to build infrastructure. Projects were often finished late and at high cost; in some cases they were never completed.

After the crisis, manufacturing growth slowed, and through to 2006 it was about the same as total GDP growth, although there was considerable variation across industrial sectors in growth of both output and exports

1 Frecaut (2004: Table 1) estimated the cumulative losses of the banking sector at almost 40 per cent of GDP by the third quarter of 1999.

(Aswicahyono, Narjoko, and Hill 2008: 31). It became clear after 1998 that at least part of the growth in manufactured exports which occurred in the decade from 1987 to 1997 was based on fragile foundations, including the unsustainable exploitation of timber to produce plywood, and draconian treatment of labour. In addition, by the early 2000s, there was abundant evidence that congested roads and ports, unreliable and expensive power supplies, and shortages of skilled workers were adding to the costs of export producers in both agriculture and manufacturing, and deterring investors, both domestic and foreign. A further set of problems related to the political changes which took place after the resignation of Suharto. Three presidents took office between May 1998 and July 2001, when the MPR removed Abdurrahman Wahid and installed Megawati Sukarnoputri. The lack of continuity in policy making aggravated an already bad investment climate. New policy initiatives such as the sweeping decentralization laws which were implemented in 2001 added to the perception that the central government had little control over much of the country.

This perception was reinforced by the rise in violent conflicts in several parts of Sumatra, Kalimantan and Eastern Indonesia, and the emergence of Islamic terrorist groups with international links whose bombing campaigns caused tragic loss of life in Bali and Jakarta. President Megawati was thought to be relying more heavily on the military to maintain order, often by repressive means. She also sought support from organized labour by introducing laws which increased minimum wages and made it more difficult and expensive for firms to dismiss workers. These policies further deterred foreign investors, who pointed out that labour costs were higher in Indonesia than in China, Vietnam, and Cambodia. The higher costs were not compensated by higher productivity; the educational and skill level of much of the labour force remained low.

By 2004 when the first direct presidential elections were held, all these problems were being extensively analysed in the Indonesian, the regional and the international press, as well as in academic studies and reports by international agencies. It was argued that Indonesia, in contrast to Thailand, Malaysia and Singapore, was “not participating vigorously” in the new regional production networks which were evolving across East and Southeast Asia (Aswicahyono, Narjoko, and Hill 2008: 18; Lipsey and Sjöholm 2011: 56-57). Although Indonesia's share of world manufactured exports increased between 1994/5 and 2006/7, its share of several categories was below Malaysia and Thailand (Athukorala and Hill 2010: Table 7). The blame was placed on poor logistics and cumbersome customs procedures, as well as inadequate investment in education and skills training. Some Indonesian commentators were blunter, and pointed out that corruption has become

worse than under Suharto. On a range of economic, social and governance indicators it appears that Indonesia has been falling behind not just China but also economies such as Vietnam and India which in the early 1990s had been well behind Indonesia.

Few observers of Indonesian economic performance in the early years of the 21st century placed the blame for Indonesia's slow recovery from the Asian crisis on external threats, whether from China or elsewhere. It seemed obvious that the key problems were internal, and included political instability, rising terrorism, deteriorating infrastructure, and stricter labour legislation all of which had caused a slowdown in FDI inflows into Indonesia. This slowdown would have occurred anyway, regardless of developments in China.² While most analysts agreed that Chinese exports of textiles, garments and footwear were displacing those from both Indonesia and the Philippines in OECD markets, the solution seemed clear; these countries would either have to implement reforms to make their labour-intensive manufactures more competitive in world markets, or they would have to develop new export industries, taking advantage of growing demand in both China and other parts of the world for resource-based products.

In fact the years from 2004 to 2010 have seen considerable improvement in Indonesia's export performance. Between 2003 and 2010, Indonesian exports more than doubled in terms of nominal US dollars (Table 3). Part of this increase was due to price increases for important exports such as oil and gas and vegetable oils, but part was also the result of quantity increases. Only 20 per cent of the increase in export value between 2003 and 2010 came from oil and gas, and another 23 per cent from other mining products, including coal. Much of the rest of the growth came from manufactures including processed vegetable oils.

Over these seven years, Indonesian exports to China grew more rapidly than total exports, and accounted for around twelve per cent of the total growth in dollar terms. By 2009, coal was the most important single export, followed by palm oil, gas, crude petroleum, and crumb rubber. Together these five products accounted for around 58 per cent of total exports to China in value terms in 2009 (Table 4).

2 For a discussion of the performance of Indonesian exports from 1980 to 2004, and comparisons with other parts of Southeast Asia see Athukorala 2006.

Table 3: Exports from Indonesia by Country of Destination (USD Billion)

Year	Total	Japan	China	Singapore
2003	61.06	13.60	3.80	5.40
2004	71.58	15.96	4.60	6.00
2005	85.66	18.05	6.66	7.84
2006	100.80	21.73	8.34	8.93
2007	114.10	23.62	9.68	10.50
2008	137.02	27.74	11.64	12.86
2009	116.51	18.57	11.50	10.26
2010	140.95	25.17	13.63	12.50

Note: Data for 2010 are preliminary.

Source: Central Board of Statistics 2009, 2011.

Table 4: Commodity Breakdown of Indonesian Exports to China: 2003 and 2009 (USD Million)

	2003	2009
Total	3,800.0	11,499.3
Of which:		
Coal	17.3	2,071.7
Palm oil	318.3	1,628.6
Crude petroleum	727.2	1,283.3
Liquified gas	110.0	1,040.4
Crumb rubber	82.0	657.1
Copper products	91.1	308.8
Petroleum products	148.6	255.5
Paper	197.6	157.5
Nickel	0	152.0
Copper ore	63.2	131.5
Electrical products	93.1	116.3
Plywood	134.6	48.3

Source: Central Board of Statistics 2006, 2010.

In common with other ASEAN countries, Indonesia exports fell in US dollar terms in 2009, as the full effects of the global downturn were felt both on prices and on demand, but there was a strong recovery in 2010. Indonesian exports to China were only slightly lower in US dollar terms in 2009 than in 2008, and there was some growth in 2010 (Table 3). By 2009, China had become Indonesia's second largest export market after Japan, and had overtaken Singapore. On the import side, growth between 2003 and 2010 was also very rapid, with only a slight decline in value terms in 2009 (Table 5). By 2010, Chinese imports to Indonesia in US dollar terms had overtaken those from both Singapore and Japan. They far outstripped imports from

both the EU and the NAFTA countries. The balance of trade between Indonesia and China, which had been running in Indonesia's favour in the earlier part of the decade had turned in China's favour after 2008.

Table 5: Imports to Indonesia by Country of Destination (USD Billion)

Year	Total	Japan	China	Singapore
2003	32.55	4.23	2.96	4.16
2004	46.52	6.08	4.10	6.08
2005	57.70	6.91	5.84	9.47
2006	61.07	5.52	6.64	10.03
2007	74.47	6.63	8.56	9.84
2008	129.20	15.13	15.25	21.79
2009	96.83	9.84	14.00	15.55
2010	135.61	16.96	20.42	20.24

Note: Figures for 2010 are preliminary.

Source: Central Board of Statistics 2009, 2011.

What was Indonesia importing from China? In 2009, around half of Chinese imports were in the machinery and transport equipment category; the second largest category was other manufactures, followed by chemicals (Table 6). In these three categories, China was running a large trade surplus with Indonesia. Imports of machinery were dominated by power generating and telecommunications equipment. It is probable that Chinese imports in these types of machinery were associated with the investments made by Chinese firms in the power and gas sectors. Some machinery imports might also have displaced imports from more advanced countries such as Japan or Germany. In this sense, they can be seen as a net gain to Indonesia, rather than displacing local production. But the pattern of trade with China which had emerged by 2009 was clearly one of exchanging unprocessed or semi-processed primary products for imports of manufactures. The implications of this are discussed further below.

The rapid growth in Indonesia's export and import trade with China over the 2000s has been mirrored in China's trade with other ASEAN countries. Between 2004 and 2008, bilateral trade between China and the ASEAN countries as a group more than doubled, and was estimated by the ASEAN Secretariat to have reached USD 231.12 billion by 2008, although there was some contraction in 2009, given the overall decline in world trade in that year.

Table 6: Indonesia's Exports to and Imports from China by Category: 2009 (USD Million)

SITC Category	Exports	Imports
0. Food & Live Animals	173.6	756.8
1. Beverages & Tobacco	2.9	143.6
2. Crude, inedible materials	2,139.9	118.3
3. Mineral fuels & Lubricants	4,658.8	535.1
4. Animal, vegetable oils, fats etc.	2,009.4	117.5
5. Chemicals, related products	747.4	1,582.4
6. Manufactured goods	909.0	2,743.9
7. Machinery & Transport Equipment	742.0	7,182.7
8. Miscellaneous manufactures	116.3	857.9
TOTAL	11,499.3	14,002.2

Source: UN COMTRADE 2010.

By 2009, China had become the largest trading partner of the ASEAN-10, overtaking the EU, Japan and the USA. In that year the ASEAN-10 accounted for 8.8 per cent of China's exports and 10.6 per cent of imports, although the percentage for Indonesia was much lower at 1.2 per cent and 1.4 per cent respectively. In ASEAN as a whole, the value of exports and imports was balanced, and Malaysia, Brunei, the Philippines and Thailand ran trade surpluses. The other countries in the region were running deficits which were substantial in Myanmar, Cambodia, Vietnam and Singapore (National Bureau of Statistics of China 2010: 238).

Since the early 2000s, there has also been an increase in Chinese investment in the ASEAN countries. The estimates of Scissors (2011) show that cumulative non-bond investment outflows from China to Indonesia in the years from 2005 to 2010 amounted to USD 9.8 billion, which made Indonesia the eight largest recipient of Chinese non-bond investment over these years, after Australia, the USA, Nigeria, Iran, Brazil, Kazakhstan and Canada. It received more investment than any other ASEAN country, including Singapore.³ Much of this outward investment in all the recipient countries was in the mineral, oil, gas and power sectors. This was certainly the case in Indonesia where the largest investors from China were power,

3 Chinese outward investment data are extremely difficult to interpret, given the fact that a high percentage goes to Hong Kong, the Cayman Islands and the British Virgin Islands. It is widely suspected that much of this goes back to China. For a discussion of the data see Schüler-Zhou and Schüller 2009. While some of the investment to Hong Kong may end up in Southeast Asia, it has also been argued that in Vietnam and Cambodia, some investment registered as Chinese is in fact owned by companies in Taiwan, Hong Kong or Macao. See Kubny and Voss 2010.

gas, energy and steel companies.⁴ By 2009, the flow of Chinese investment into Indonesia appeared to have slowed; in that year Indonesia was not in the top twenty recipients of Chinese investment, although both Singapore and Myanmar were (Salidjanova 2011: Table 1). ASEAN investment into China also continued to grow especially from Singapore.⁵

The ASEAN-China FTA

Discussions about enhanced economic cooperation between China and ASEAN began in 2000, at the ASEAN-China summit in that year. It was decided to move towards a formal Free Trade Area, incorporating six of the ten ASEAN countries in 2010, with Vietnam, Laos, Cambodia and Myanmar joining in 2015. The formal commencement of the ASEAN-China Free Trade Agreement (ACFTA) on 1 January 2010 was greeted with great enthusiasm at the official level in China and in some multilateral bodies. The official Chinese view was that “China and ASEAN enjoy geographic advantage in their economic cooperation, and their economies are highly complementary to each other”. Senior officials in the Asian Development Bank were quoted as arguing that ACFTA was an important vehicle for trade-led recovery in the Asia-Pacific region. It was also pointed out that ACFTA presented an opportunity for the ASEAN countries to “latch on to China’s production networks” and sell to Chinese consumers (see Macan-Markar 2009). The reaction in ASEAN was more muted, although the ASEAN Secretary-General stated that the free trade area “will benefit both sides and help lift the world economy out of the crisis”.

In one sense the official enthusiasm around a free trade area between China and the ASEAN-6 might seem rather odd, given that all these countries were already WTO members, and as such supposedly committed to non-discriminatory free trade. Most of the supporters of the ACFTA have made little attempt to spell out exactly what the benefits would be, either to China or to the various ASEAN countries. Indeed some commentators have suggested that the business communities in ASEAN and China played little role in creating the ACFTA, which appeared to be largely driven by political factors (Ravenhill 2010). At the same time, voices were raised in the ASEAN region which were much less supportive of the ACFTA. In the Philippines, fears were expressed that it would simply legalise the widespread smuggling of footwear, garments, shoes, and other manufactures and

4 For a complete breakdown of all Chinese overseas investment deals between 2008 and 2010 see Salidjanova 2011, appendix 1.

5 See the paper by Krislert Samphantharak in this issue.

agricultural products which has already placed considerable pressure on domestic producers (see Bello 2009). The Indonesian government, no doubt concerned about the domestic implications of the ACFTA, formally lodged a letter on 14 January 2010, asking the ten ASEAN nations to defer the implementation until January 2011, although this did not happen.

Part of the concern in both Indonesia and the Philippines resulted from a fear that there might be a repeat of the Thai experience, when the so-called “early harvest” experiment during the Thaksin government caused problems for Thai farmers. In Thailand, tariffs on around two hundred fruits and vegetables between Thailand and China were removed. This resulted in a flood of products from China into Thailand, but Thai farmers found that exports of their products into China were still being subject to various tariff and non-tariff barriers. As tariffs are reduced or removed on a much broader range of agricultural and manufactured products, there is an expectation in several ASEAN countries that China will continue with what the outspoken Chinese economist, Hu Angang has termed China’s “half-open” model. This means that China will flood the ASEAN countries with Chinese products sold at extremely low prices, while taking in return only those products, mainly unprocessed raw materials, which are needed for China’s accelerated industrialization. The fact that many Chinese producers had by early 2010 large unsold stocks of manufactures as a result of slowing world demand added to the concerns in ASEAN that these products will be dumped in Southeast Asia at below cost prices. While it is easy to dismiss some of these claims as attempts by high-cost local producers to claim protection against cheaper imports, whether from China or elsewhere, the problem of dumping cannot be dismissed out of hand. The ACFTA agreement did not appear to include any formal procedures for settling disputes; in the longer term these will have to be introduced.

Indonesian fears were expressed in an opinion piece in Indonesia’s leading English-language paper, published in October 2010, which pointed out that “most people are of the opinion that Indonesia’s agricultural products and manufacturing goods are extremely uncompetitive against China’s.” It went on to argue that instead of seeing the ASEAN-China Free Trade Agreement as an instrument to strengthen the interdependence of the ASEAN region with China, many Indonesians see it as leading to “cutthroat competition that will have negative impacts on the development of Indonesian economic capabilities in the long term” (*Jakarta Post* 2010). Others view Chinese policies as essentially neo-colonial; in its hunger for raw materials, China is in effect seeking to re-impose colonial patterns of trade on Southeast Asia. It is too early to tell if these fears are justified or not, but they appear

to reflect widely held beliefs in Indonesian business, media and political circles.

China, ASEAN and the East Asia 15

The last two decades of the twentieth century witnessed the peaceful and successful integration of China into the East Asian and the wider global economy. This process, largely market driven, is continuing into the 21st century, and has brought benefits to many tens of millions of Asians in terms of greater employment opportunities, and to even greater numbers in other parts of the world in terms of cheap consumer goods. Inevitably there have been repercussions for producers of traded goods in other parts of Asia, and in other parts of the world. But the rise of China, and the robust growth in the global economy as a whole until 2008, presented the ASEAN economies with a number of opportunities to integrate themselves into global production networks. These opportunities have led to the rapid growth of plants, many Japanese-owned, producing vehicles and vehicle parts, and computer components in Thailand. In the Philippines, exports of electronic products increased rapidly, mainly as a result of investment by Japanese and American multinationals (Haltmeir et al. 2007: 32-35).

The evidence certainly does not support the argument that the rise of China is wiping out the industrial sectors of all the ASEAN economies. Several of them have benefited from the growth of “Factory Asia”, where “billions of different parts and components from plants spread across a dozen nations” are assembled and dispatched to markets all over the world (Baldwin 2006). According to one recent study, trade in parts and components has been expanding more rapidly than final goods trade in recent years, and this trend has been “proportionately larger in East Asia, in particular in ASEAN, compared to North America and Europe” (Athukorala 2008: 505). This author has also argued that the argument that China’s rise would “crowd out” labour-intensive exports from other parts of Asia is not backed up by the evidence. To the extent that exports of textiles, footwear, garments etc. have been falling in recent years, it has happened in the high-wage Asian economies as a result of their own changing comparative advantage (Athukorala 2009: 260). Even in Indonesia, where some of the traditional labour-intensive industries have faced difficulties since 1998 for the reasons already discussed, garment, footwear and electronics exports have shown some increase in dollar terms, at least until 2008. In that year garment and footwear exports were valued at almost USD 8 billion, while exports of electrical and audio-visual equipment amounted to over USD 8 billion (Central Board of Statistics 2009: 515-21).

In contrast to some of its ASEAN partners, especially Singapore, Indonesia has not been enthusiastic in forming bilateral free trade arrangements with other countries, either in Asia or elsewhere. Its trade share with other ASEAN countries has risen since the 1990s, and by 2005 it was estimated that around 23 per cent of Indonesia's total trade was with other ASEAN countries, especially Singapore, Malaysia and Thailand.⁶ Around 62 per cent was with the "East Asian 15" which includes ASEAN, China, Japan, Taiwan, South Korea and Hong Kong. Already in 1990, Indonesia was doing 58 per cent of its trade with these countries, which was much higher than the average for all 15 in that year. Although the intra-regional trade share increased between 1990 and 2005 for the East Asian 15, Indonesia continued to have a higher than average share (Table 7). In this sense it could be argued that Indonesia has been more deeply integrated into the greater East Asian trade network over a longer period of time than many other economies in the region. Indeed China's trade share with other countries in the East Asian 15 actually fell between 1990 and 2005. This reflects the fact that after China joined the WTO, its trade with both the USA and the EU grew rapidly.

Table 7: Percentage of Total Trade Taking Place in Regional Groupings: 1990 and 2005

Country/Region	ASEAN-10		ASEAN Plus 5	
	1990	2005	1990	2005
Indonesia	9.3	22.9	58.1	62.1
Malaysia	24.3	25.4	55.8	58.2
Philippines	9.3	18.1	42.1	61.3
Singapore	19.5	31.3	47.4	63.3
Thailand	12.6	20.0	48.5	55.8
Vietnam	16.6	21.2	38.2	61.3
ASEAN-10	17.0	25.5	n.a	n.a
China	n.a	n.a	57.1	43.9
Japan	n.a	n.a	28.8	45.6
ASEAN plus 5	n.a	n.a	41.1	52.7

Source: Chia 2007: 3.

Other studies of East Asian trade confirm the argument that already in 1990 the proportion of total trade of East Asian countries that took place within the region was quite high, and the increase between 1990 and 2005 was relatively modest (Park and Shin 2009: 136). Perhaps surprisingly in view of

6 In 2010, around 25 per cent of Indonesia's export and import trade was conducted with other ASEAN countries.

their statistical results, Park and Shin argued that East Asia in the early years of the 21st century was actually de-coupling from the rest of the world economy, and especially from trade and investment ties with the USA. They are advocates of more institutional support for East Asian economic integration along EU lines. Other researchers also advocated the formation of East Asia-wide Free Trade Agreements (FTAs), mainly as a means of counteracting the probable negative effects of a “noodle bowl” tangle of bilateral FTAs, which was attracting much critical comment by the early 2000s. Some observers felt that these bilateral deals might end up harming the successful process of market-driven integration which has taken place since 1980 (Chia 2007; Baldwin 2006; 2008). Although Chia (2007: 30-31) argued that Baldwin’s pessimism about the fragility of East Asian regionalism is somewhat misplaced, both she and Baldwin appeared to support an ASEAN plus 3 FTA. This would present the best opportunity for the region as a whole, although the ASEAN countries are still faced with the twin challenges of completing their own single market, and also with finalising the ASEAN-China FTA.

Given Indonesia’s high trade share with other countries in East and Southeast Asia, it would seem to be in Indonesia’s long-term interest to push for progress on an East Asia-wide free trade area, and for progress on initiatives to secure greater monetary cooperation. After the 1997/98 crisis, many Indonesians together with Thais, Koreans and Malaysians realized that they could not depend on the Bretton Woods institutions to assist them in a major crisis. Countries less affected by the 1997/98 crisis including China and Vietnam drew the same conclusion. The events of 2008/09 will only strengthen the conviction that all the economies of East and Southeast Asia have much to gain from closer cooperation, even if such cooperation also entails short-term costs to some producers in the region. But how should this cooperation proceed? The inauguration of the ACFTA has brought to light problems and grievances which are almost certainly going to vex relationships between the ASEAN countries and China for years and possibly decades to come. Given that the free trade area has come into being without any robust dispute resolution procedures, it is far from clear how disputes over dumping of products will be resolved.

The official enthusiasm in China for the ACFTA has raised suspicions in several parts of ASEAN, including Indonesia, that the Chinese will use it to their own advantage. On the import side, they will continue to press for access to Southeast Asia’s raw materials while continuing to impose barriers to imports from ASEAN of both agricultural and manufactured goods which might threaten their own producers. These suspicions are in turn based on fears about the motivations of Chinese foreign economic policy. Is

China treating the major ASEAN governments in the same way that it has dealt with several regimes in Africa, whose governments have granted China access to oil, mineral resources, and even agricultural land, on favourable terms in exchange for loans and other forms of economic assistance? Certainly this has been the case in Myanmar, where Chinese economic support has been, and continues to be, essential for the survival of the regime. Indonesia, along with countries such as Thailand, Malaysia and the Philippines, are far from being client states of China, and economic relations should be conducted on the basis of mutual benefit, and respect for WTO procedures.

But at the same time, it is clear that China's growing export power has forced several ASEAN countries to re-evaluate their longer-term comparative advantage. The ASEAN-4 (Thailand, Malaysia, the Philippines and Indonesia) all made progress in increasing the share of manufactured exports in total exports over the decades from the 1970s to the 1990s, although exports of oil and gas and other mineral and agricultural products remained important in Indonesia, even after the reforms of the late 1980s led to rapid growth of exports of manufactures. Although it is true that Indonesia after the crisis of 1997/98 has not been as successful as Thailand in benefiting from the growth of trade in parts and components, it has continued to develop land-based export products such as palm oil, while at the same time taking advantage of growing world demand for both gas and other mineral products including coal. In addition, as this paper has argued, exports of garments, footwear and electrical products have increased in recent years, in spite of increased competition from China and other exporters including Pakistan.

But it is undeniable that fears of current Chinese intentions regarding the ACFTA have reinforced long-standing resentments on the part of indigenous Southeast Asians concerning the economic role of their own Chinese minorities. A pessimistic view of the future is that discontent on the part of both industrial and agricultural workers over "unfair" Chinese competition in Indonesia could spill over into violence against the Chinese minority, especially if trading companies owned by Indonesians of Chinese origin are seen to be benefiting from sales of merchandise originating from China. The greater political openness in the post-Soeharto era has encouraged some politicians to embrace economic nationalism in its more extreme form, with strong anti-Chinese undertones. It is quite possible that these elements will exploit resentments concerning the outcomes of the ACFTA. This in turn could lead to tensions within ASEAN, which could slow progress towards an ASEAN single market, which will remain the primary objective of ASEAN foreign economic policy over the next few years. A more optimistic view is that Indonesian producers of a range of primary and manufactured

products will benefit from surging Chinese demand, while Indonesian producers and consumers will benefit from cheaper imports of capital equipment and consumer goods. Which view will prevail in coming years is difficult to predict.

References

- Aswicahyono, Haryo, Dionisius Narjoko, and Hal Hill (2008), *Industrialization after a Deep Economic Crisis: Indonesia*, Working Paper No 2008/18, Canberra: Australian National University, Arndt-Corden Division of Economics, College of Asia and the Pacific.
- Athukorala, Prema-Chandra (2009), The Rise of China and East Asian Export Performance: Is the Crowding-Out Fear Warranted?, in: *The World Economy*, 32, 2, 234-266.
- Athukorala, Prema-Chandra (2008), Singapore and ASEAN in the New Regional Division of Labour, in: *Singapore Economic Review*, 53, 3.
- Athukorala, Prema-Chandra (2006), Post-crisis export performance: the Indonesian experience in regional perspective, in: *Bulletin of Indonesian Economic Studies*, 42, 2, 177-211.
- Athukorala, Prema-Chandra and Hal Hill (2010), Asian trade; long-term patterns and key policy issues, in: *Asian-Pacific Economic Literature*, 24, 2, November, 52-82.
- Athukorala, Prema-Chandra and Swarnim Wagle (2011), Foreign Direct Investment in Southeast Asia: Is Malaysia Falling Behind?, in: *ASEAN Economic Bulletin*, 28, 2, 115-133.
- Baldwin, Richard (2008), The Spoke Trap: Hub-and-Spoke Bilateralism in East Asia, in: Barry Eichengreen, Charles Wyplosz, and Yung Chul Park (eds.), *China, Asia and the New World Economy*, Oxford: Oxford University Press.
- Baldwin, Richard (2006), *Managing the Noodle Bowl: The Fragility of East Asian Regionalism*, Working Paper No 5561, London: Centre for Economic Policy Research.
- Bello, Walden (2009), *The China-ASEAN Free Trade Area: Propaganda and Reality*, online: <<http://focusweb.org>> (9 December 2009).
- Central Board of Statistics (2011), *Trends of the Selected Socio-Economic Indicators of Indonesia*, February, online: <www.bps.go.id> (15 May 2011).
- Central Board of Statistics (2010), *Statistical Yearbook of Indonesia, 2010*, Jakarta: Central Board of Statistics.
- Central Board of Statistics (2009), *Statistical Yearbook of Indonesia, 2009*, Jakarta: Central Board of Statistics.
- Central Board of Statistics (2006), *Statistical Yearbook of Indonesia, 2006*, Jakarta: Central Board of Statistics.

- Chia, Siow-Yue (2007), Whither East Asian Regionalism?: An ASEAN Perspective, in: *Asian Economic Papers*, 6, 3, 1-36.
- Frecaut, Olivier (2004), Indonesia's Banking Crisis: A New Perspective on \$50 billion of Losses, in: *Bulletin of Indonesian Economic Studies*, 40, 1, April, 37-57.
- Haltmaier, Jane T. et al. (2007), *The Role of China in Asia: Engline, Conduit or Steamroller?*, Board of Governors of the Federal Reserve System, International Finance Discussion Papers, Number 904, September.
- Jakarta Post* (2010), 27 October.
- Kubny, Julia and Hinrich Voss (2010), *China's FDI in ASEAN: Trends and impact on host countries*, Bonn: German Development Institute, and Leeds University Business School.
- Lipsey, Robert E. and Fredrik Sjöholm (2011), Foreign Direct Investment and Growth in East Asia: Lessons for Indonesia, in: *Bulletin of Indonesian Economic Studies*, 47, 1, April, 35-63.
- Macan-Markar, Marwaan (2009), *ASIA: China-ASEAN Free Trade Area Sparks Cautious Optimism*, online: <<http://ipsnews.net>> (9 December 2009).
- National Bureau of Statistics of China (2010), *China Statistical Yearbook 2010*, No 29, Beijing: China Statistics Press.
- Park, Yung Chul and Kwanho Shin (2009), Economic Integration and Changes in the Business Cycle in East Asia: Is the Region De-coupling from the Rest of the World?, in: *Asian Economic Papers*, 8, 1, 107-140.
- Ravenhill, John (2010), The 'new East Asian regionalism': A political domino effect, in: *Review of International Political Economy*, 17, 2, May, 178-208.
- Ravenhill, John (2006), Is China an Economic Threat to Southeast Asia?, in: *Asian Survey*, 46, 5, 653-674.
- Salidjanova, Nargiza (2011), *Going Out: An Overview of China's Outward Foreign Direct Investment*, USCC Staff Research Report, Washington: U.S.-China Economic and Security Review Commission.
- Schüler-Zhou, Yun and Margot Schüller (2009), The internationalization of Chinese companies, in: *China Management Studies*, 3, 1, 25-42.
- Scissors, Derek (2011), *China Global Investment Tracker*, Washington: Heritage Foundation, online: <www.heritage.org/research/reports/2011/01/china-global-investment-tracker-2011> (20 May 2011).
- Tongzon, Jose L. (2005), ASEAN-China Free Trade Area: A Bane or Boon for ASEAN Countries, in: *The World Economy*, 28, 2, 191-210.
- UN COMTRADE (2010), *United Nations Commodity Trade Statistics Database*, New York: UN comtrade, online: <<http://comtrade.un.org/>> (15 December 2010).
- UNCTAD (2010), *World Investment Report*, Geneva: UNCTAD.

Woo, Wing Thye (2006), The Economic Impact of China's Emergence as a Major Trading Nation, in: Lok Sang Ho and Robert Ash (eds.), *China, Hong Kong and the World Economy: Studies on Globalization*, London: Palgrave.