

# OPPORTUNITIES AND THREATS OF ASEAN ECONOMIC COMMUNITY FOR MICRO, SMALL AND MEDIUM ENTERPRISES IN EAST JAVA

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#### Article History

Received: 23-08-2023 Revision: 26-08-2023 Accepted: 26-08-2023 Published: 27-08-2023 Abstract. The implementation of the ASEAN Economic Community (AEC) in 2015 is aimed to improve economic relations in ASEAN. The AEC required provisions for the trade liberalization that might impact positively or negatively for entrepreneurs. This article is aimed to describe the opportunities and threats of AEC for Micro, Small and Medium Enterprises (MSMEs) in East Java. If AEC has been implemented for more than five years, AEC should have made a real contribution to MSMEs in East Java. In fact, there were many MSMEs in East Java who don't even know what AEC is. To analyze it, the author used the concept of economic integration by Bela Balassa. The author used a type of descriptive research with a qualitative approach. The data used in this study are primary and secondary data. Based on the findings, the opportunities for AEC for MSMEs in East Java are product standardization and market access. Meanwhile, AEC's threats to them are product similarity, foreign investment, and the free flow of goods. Even so, both do not have a significant impact on MSMEs in East Java because the target sales of MSMEs in East Java are mostly for the domestic market.

Keywords: ASEAN Economic Community, MSMEs, East Java

Abstrak. Pemberlakuan ASEAN Economic Community (AEC) pada tahun 2015 bertujuan untuk meningkatkan hubungan ekonomi di ASEAN. AEC memerlukan ketentuan liberalisasi perdagangan yang mungkin berdampak positif atau negatif bagi pengusaha. Artikel ini bertujuan untuk mendeskripsikan peluang dan ancaman AEC bagi Usaha Mikro, Kecil dan Menengah (UMKM) di Jawa Timur. Jika MEA sudah diterapkan lebih dari lima tahun, seharusnya AEC dapat memberikan kontribusi nyata bagi UMKM di Jatim. Faktanya, masih banyak UMKM di Jawa Timur yang belum mengetahui apa itu AEC. Untuk menganalisanya penulis menggunakan konsep integrasi ekonomi yang dikemukakan Bela Balassa. Penulis menggunakan jenis penelitian deskriptif dengan pendekatan kualitatif. Data yang digunakan dalam penelitian ini adalah data primer dan sekunder. Berdasarkan temuan, peluang AEC bagi UMKM di Jawa Timur adalah standarisasi produk dan akses pasar. Sedangkan ancaman AEC terhadapnya adalah kesamaan produk, penanaman modal asing, dan arus bebas barang. Meski begitu, keduanya tidak memberikan dampak signifikan terhadap UMKM di Jatim karena target penjualan UMKM di Jatim sebagian besar untuk pasar dalam negeri.

Kata Kunci: ASEAN Economic Community, UMKM, Jawa Timur

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#### **INTRODUCTION**

Micro, Small and Medium Enterprises (MSMEs) have potentials, roles, and positions, which are considered very strategic in achieving national development goals. In East Java, the large contribution of MSMEs to the regional economy can be seen from the economic growth rate of 7.22% which was largely boosted by the MSME sector. In fact, of East Java's GRDP (Gross Regional Domestic Product). which reached up to IDR 1,000 trillion in 2011, 54% was obtained from 4.2 million MSMEs in this province.(Binarto et al., 2013). The ASEAN Economic Community (AEC) represents an economic-based regional integration model that has been implemented by 10 ASEAN member countries since 2015. One of the programs from AEC is implementing trade liberalization to create a free market in the Southeast Asian region. The trade liberalization implemented in the AEC provides improvement of the ASEAN Free Trade Area (AFTA) agreement that was implemented by ASEAN previously, namely in 1992. The implementation of AFTA requires ASEAN countries to reduce their trade tariffs on goods to 0-5%.(Ministry of Home Affairs, 2002).

The Indonesian government's policy to participate in implementing the AEC is not without any reason. The AEC single market is designed as an enforcement of trade liberalization, so that the volume of regional trade will increase, then it would have a domino effect to Indonesia's economic growth in the future. With minimal tariffs and trade barriers, business actors can enjoy export convenience, starting from the point of view of taxes, quotas, permits, and so on. What's more, in the current era of globalization, advances in information and communication technology can help facilitate trade transactions in the region because sellers and buyers only need to have smartphone and an internet network to make transactions, or commonly referred to as e-commerce. Such regional trading facilities will be a trigger for the growth and development of Micro, Small and Medium Enterprises (MSMEs) in Indonesia. (People Matters Global, 2019)<sup>.</sup>

If on the one hand AEC brings positive impacts, then on the other hand it also brings negative impacts. The reduction in tariffs in the single market scheme could result in an increase in the number of imported goods in the country. The rush of imported goods makes the existence of domestic producers increasingly threatened because these imported goods will also compete in the domestic market, with the possibility of a much lower price, a more attractive appearance or better quality. If left unchecked, domestic producers may suffer losses or even go out of business. (Perindustrian, 2015). The next effect that can be caused is a trade balance deficit. The trade balance deficit occurs because the total value of imports is greater than the total value of exports. Given that Indonesia has good market potential due to its large

population, Indonesia could become a major export target for ASEAN countries. The former Minister of Industry of the Republic of Indonesia, MS Hidayat, revealed that with the large population and geography of Indonesia, if Indonesia is entered into imported products, then Indonesia has the opportunity to become a buyer (consumptive), so it needs to be avoided.(Detik Finance, 2013).

Such conditions indicate that AEC is like having "two sides of the same coin" which creates a dilemma because it can be both an opportunity and a threat for MSMEs in East Java. If we look at the implementation of AEC which has been carried out since 2015, which means it has been more than five years, then the influence of AEC on MSMEs in East Java should be visible, both positive and negative. However, the authors found facts in the field that there are still many MSMEs in East Java who do not know everything about AEC. They only know about free trade between Indonesia and other countries, which can be seen from the increase in exports and imports, but they do not know what regime this free trade mechanism is in. In fact, Indonesia's free trade regime with other countries itself is very much, AEC is only one of them.

If analyzed using the concept of economic integration developed by Bela Balassa, AEC has fulfilled the characteristics to be said as a form of economic integration because AEC is aimed at increasing the implementation of free trade for countries in the Southeast Asian region. Even so, there is an imbalance in the AEC because according to Balassa, in economic integration in a region, there are six stages of economic integration that should be carried out by a country's economy, namely, (1) Preferential Trade Area; (2) Free Trade Areas; (3) Custom Union, (4) Common Market, (5) Economic Union; and (6) complete integration. These six stages must be carried out to achieve an increasingly integrated economy. Economic integration within ASEAN has gone through the Preferential Trade Area and Free Trade Area stage, supposedly, the next stage is the Custom Union. However, what happened to AEC was precisely the characteristics of the Common Market. That is, ASEAN has skipped a stage which will ultimately make economic integration in the AEC seem flawed.(Balassa in T. Widodo, 2016).

There have been several scientific works that also discuss AEC. Among them is Ilham Akbar's article entitled "Preparation of the East Java Provincial Government in Facing the ASEAN Economic Community (AEC) through Leading Sectors". However, Akbar's writings make the Provincial Government of East Java as the research subject, while the research subjects in this article are MSMEs which are the direct targets of the AEC free trade scheme. There is also an article from Yulia Delasari entitled "The Impact of the ASEAN Free Market (AEC) on the Growth of MSMEs in Riau Province (Bolu Kemojo Food Industry)". In contrast

to Delasari's writings, this article does not only examine one industrial commodity, but various industrial commodities that are affected by the AEC. In addition, East Java Province was chosen with the consideration that East Java is a business center for Eastern Indonesia. Furthermore, another article by Sri Maulida entitled "Opportunities and Challenges in the Development of Micro, Small Enterprises. Medium Enterprises (MSMEs) from Various Economic Aspects. Maulida's writing also discusses the two sides faced by MSMEs. Unfortunately, Maulida's writing does not specify the AEC regime as is done in this article.

This is what then makes the author feel interested in examining the opportunities and threats given by the AEC to MSMEs in East Java. AEC seems to give more threats to MSMEs in East Java considering that AEC seems flawed as a form of economic integration. This study will later be useful for the East Java Provincial Government as a reference for determining policies in dealing with the implementation of AEC in the future, bearing in mind that MSMEs in East Java make the largest contribution to the regional economy.

# METHOD

This article was written based on the results of research using a qualitative approach. According to Creswell, the purpose of qualitative research is to explore and understand the meaning of what is considered a social or human problem.(Creswell in Kusumastuti & Khoiron, 2019) Thus, the research conducted by the author requires submitting a number of detailed questions to the participants, namely MSMEs and a number of related agencies in cities in East Java, then analysing the data inductively starting from specific themes to general themes, and interpret it. Meanwhile, the type of research is descriptive, namely by describing the actual situation experienced by MSMEs in East Java as research subjects. Descriptive research is used to reveal facts, circumstances, events, phenomena, and variables that occur during research. This research provides an interpretation of the data according to the facts in the field, starting from the export activities carried out by MSMEs in East Java, to the activities they carry out in dealing with an increase in imported goods.

Data collection was carried out by visiting several cities in East Java province, namely Surabaya, Sidoarjo, Trenggalek, Pacitan, Madiun, Ngawi, Pasuruan, Probolinggo and Malang. The selection of cities was based on the consideration that MSMEs in these cities have quite high export activities with a variety of commodities. In addition, the author also used secondary data obtained from websites and online news articles. Meanwhile, the time needed to extract data is around five months, namely April to September 2021.

To analyze the data, the authors used the Miles and Huberman models. First, Data Condensation, in which the author made several simplifications related to the research focus and themes that are no longer relevant. Second, Data Presentation, the author had presented the most general description of AEC as a form of economic integration that promotes free trade in ASEAN to the main issues related to the opportunities and threats of AEC for MSMEs in East Java. Third, Verification, in which the author triangulated the data by reconfirming the statements and data that the author obtained from the MSME to the association of local economy in East Java and the local governments.

# RESULTS

#### The Role of MSMEs for the East Java Economy

MSMEs have an important role for the economy in East Java province. The average development of MSMEs in East Java is 54.34% per year and accommodates 98% of the workforce. In 2008, the number of MSMEs based on the 2006 Economic Census was 4.6 million MSME units. In 2012, the number increased to 6.8 million MSME units and contributed 54.48% to regional income or the equivalent of IDR 600 trillion. The contribution of MSMEs in East Java to regional income is reflected in the percentage of added value of East Java MSMEs to East Java's total GRDP (Gross Regional Domestic Product). In 2018 the contribution of MSMEs to East Java's GRDP was 56.93% then increased to 57.26% in 2019 and in 2020 it was 57.25%.

#### **AEC** as a Form of Economic Integration

Considering the main objectives of the ASEAN Economic Community (AEC) which include single market and production base, increasing regional economic competitiveness, equitable regional economic growth, and integration of the regional economy to the world economy, implicitly AEC can be said to be a form of economic integration. Regarding the goal of single market and production base, ASEAN realizes this by implementing free flow of five elements, namely goods, services, investment, capital and skilled labour. However, if identified from the application of the AEC in more detail, the following rules can become explicit evidence of the economic integration promoted by the AEC.(Laksanawati, 2014)

First rule, elimination of tariff barriers. The tariff barrier elimination scheme is based on the Common Effective Preferential Tariff for ASEAN Free Trade Area (CEPT-AFTA) agreement. CMLV countries (Cambodia, Myanmar, Laos, Vietnam) get preferential treatment compared to ASEAN-6 (Indonesia, Malaysia, Singapore, Thailand, Brunei Darussalam, Philippines) because there is an economic disparity between the two. The implementation of AEC is expected to be able to minimize the economic disparity between the two groups and accelerate regional integration through several provisions in the tariff barrier elimination scheme. First, the elimination of entry fees for goods except those listed on the Sensitive List (SL) and Highly Sensitive List (HSL). For ASEAN-6 no later than 2012, while for CMLV in 2015 with flexibility in 2018. Second, the elimination of entry fees for Priority Integration Sectors (PIS) products. PIS covers 12 sectors, which include (1) wood-based products; (2) automotive; (3) rubber-based products; (4) textiles and clothing; (5) agriculturally based products; (6) fisheries; (7) electronics; (8) e-ASEAN; (9) health; (10) air travel; (11) tourism), and (12) logistics services. Third, the phasing of Sensitive List products with 0-5% tariffs no later than 2010 for ASEAN-6, 2013 for Vietnam, 2015 for Laos and Myanmar, and 2017 for Cambodia.

The second rule is the elimination of non-tariff barriers. Non-tariff barriers will be abolished through several provisions. First, increasing transparency by complying with the Protocol on Notification Procedure and developing an effective Surveillance Mechanism. Second, the elimination of all non-tariff barriers no later than 2010 for ASEAN-5, 2012 for the Philippines, and 2015 with flexibility in 2018 for CMLV. Third, increase the transparency of non-tariff policy measures.

The third rule, Rule of Origin (provisions of origin of goods). Establishing a Rule of Origin adapted to the dynamics of change in the global production process to facilitate ASEAN trade and investment, expand regional production, encourage MSMEs, overcome development gaps, and increase the utilization of the CEPT-AFTA scheme. The fourth rule, trade facilities. In terms of trade facilities, countries are required to simplify, harmonize, and standardize several things, starting from processes, procedures, and information related to customs and trade. It is hoped that this will reduce ASEAN transaction costs so that it can increase competitiveness and facilitate the process of regional integration.

The fifth rule, quality assurance. In terms of standard systems, quality assurance, technical regulations, accreditation, and other procedures are aligned. In addition, improvements in technical infrastructure and testing of goods based on procedures and guidelines are recognized both regionally and internationally. Sixth rule, barriers to the service sector. In the service sector, one way is to reduce barriers to trade in priority service sectors, namely air transportation, e-ASEAN, tourism, and health in 2015. Seventh rule, foreign investment. To increase ASEAN's competitiveness in Foreign Direct Investment (FDI), the investment regulations are made to be free and open. Improvement in investment protection is also

conducted to provide a better business climate for investor. Procedures, regulations, rules and investment policies are regenerated to be more transparent, predictable and consistent.

# DISCUSSION

Based on the Bela Balassa economic integration concept, ASEAN has missed one stage of economic integration. After going through the Preferential Trade Area and Free Trade Area stages, ASEAN should have implemented the Custom Union stage first. However, the characteristics of economic integration in AEC represent the stage of the Common Market. This opens opportunities for countries outside ASEAN members to take advantage of this gap, namely by first exporting goods to ASEAN member countries that set the lowest tariffs, and then exporting them to other ASEAN member countries. Economic integration in the form of a Common Market promoted by AEC gives freedom to factors of production to move easily between countries, such as factors of production in the form of capital and labor.

Even though the discrepancy with Bela Balassa's concept of economic integration casts doubts on the future of AEC, ASEAN countries have their own way of integrating the economy, and they call this principle as the "ASEAN Way". The ability of AEC to operate as a Common Market without uniformity of tariffs for countries outside ASEAN members has been questioned by many parties. Even so, an economic observer from Gadjah Mada University, Prof. Tri Widodo, believes that the theory put forward by Balassa has been well tested, with the European Union as an example. The European Union has passed each stage of economic integration well. This makes the economic integration of the European Union considered as the best if compared to the others. Therefore, even though there are pros and cons regarding policy discrepancies with theory, AEC will still be implemented with the belief of the "ASEAN Way". The truth of the theory of economic integration by Balassa and the "ASEAN Way" can only be proven by later developments and answered by time.(Yudhawirawan, 2017)

# **Opportunities of AEC for MSMEs in East Java**

AEC provides opportunities for MSMEs in East Java through free trade provisions that lead to product standardization. When AEC is implemented, MSMEs are asked to produce goods according to predetermined standards. If MSMEs can carry out production activities to produce standardized products, then MSMEs can increase the competitiveness of their products or even become suppliers of needs for large industries in other ASEAN member countries. In relation to product standardization provisions, MSMEs in Surabaya, Sidoarjo, Pasuruan, and Probolinggo agree that product standardization because of AEC implementation allows them to gain new knowledge to make their products better so that they have high competitiveness. For example, the owner of a small chip product business in Probolinggo said that provisions regarding product standardization made small business owners learn new technologies.(Apud, 2019) They no longer pack their products with just plain plastic, but rather pack them with rather thick plastic with attractive shapes and are branded with pictures. In line with Probolinggo, the owner of a medium-sized furniture product business in Pasuruan also said that from product standardization, furniture entrepreneurs know about the latest technologies used to process wood. Meanwhile, in other cities such as Ngawi and Magetan, product standardization is not really felt because they do not understand the mechanism of free trade in the AEC.

In fact, the success of MSMEs in adapting the AEC provisions regarding product standardization cannot be separated from the government's role. When the AEC was implemented, the local government in each city in East Java followed up by providing training to MSMEs to be able to improve the quality and sales of their products. The training is conducted regularly, is free of charge, and can be accessed by all MSMEs. Thus, it is from here that MSME can make product standardization an opportunity for them, not a threat that hinders their exports. Apart from standardization, there is also other opportunity from AEC for MSMEs in East Java. The opportunity is market access. Theoretically, as a form of economic integration, AEC offers expansion of market access for business actors. Business actors in one ASEAN member country will be able to easily sell their products to other ASEAN member countries. This can be seen in Sidoarjo, where small business owners of footwear products (shoes or sandals) explained that their products can now be exported to several neighbouring Indonesian countries such as Malaysia and Thailand, without having to be complicated by the application of tariffs or high customs taxes or other export-import regulations.(Hadi, 2019)

AEC's opportunities in terms of expanding market access in ASEAN member countries can be felt by all MSMEs in East Java, in Sidoarjo. However, many MSMEs in other cities and regencies say that they are not targeting foreign market but tend to target the domestic market. From several cities in the East Java Region, the expansion of market access is more in demand by MSMEs located in big cities such as Surabaya, Sidoarjo and Malang because they have quite high export activity. Meanwhile, other cities prefer to be oriented towards the domestic market even though they also export their products on a small scale.

## Threats of AEC to MSMEs in East Java

The threats of AEC for MSMEs in East Java are directly proportional to the opportunities it provides. Apart from being an opportunity, free trade also poses a threat when Indonesia is flooded with imported goods from other ASEAN member countries. MSMEs in Trenggalek, Pacitan, Madiun, and Ngawi stated that the impact seen in their eyes was the similarities between imported products and the products they sold. When viewed based on the characteristics of ASEAN member countries, the threat of product similarity is indeed not a surprising thing. The reason is, the ASEAN member countries are in the same region, which means that they have similar geographical conditions as well. They have similar natural resources, so the products produced are also around agricultural, plantation and fishery products.

Problems then arise when the similarity of imported products with local is followed by the cheap price of these imported products. With the regulation regarding the elimination of tariff barriers, products from other countries that enter Indonesia can be sold at the same price as local products or even cheaper. One of them is the owner of a medium-sized garment product business in Madiun who admits that handicrafts made by local residents are rivaled by similar products from China which are sold at much cheaper prices. (Wahyuni, 2019) An interesting point that needs to be underlined here is that these MSMEs view imported products that are their competitors as products from China, not from ASEAN member countries. Then, by looking at the tendency of the Indonesian people to be consumptive, if local products and similar imported products are juxtaposed, then imported products are much more in demand because they are considered more prestigious and cheaper when compared to local products.

The data that the author has described regarding the opportunities and threats of AEC for MSMEs in East Java mentioned above ultimately boils down to the fact that although AEC provides real opportunities and threats for MSMEs in East Java, these two things do not have a significant impact on them. The AEC opportunities do not have a significant impact because not many MSMEs in East Java export their products, they tend to sell their products in the domestic market rather than export them. The significant impact is only felt on MSMEs that export products made from local ingredients or those that have unique characteristics. Meanwhile, the AEC threats do not have a significant impact because MSMEs in East Java suffer more from imported goods from China, not imports from ASEAN member countries.(Wahyuono, 2019)

### CONCLUSION

The ASEAN Economic Community (AEC) provides opportunities as well as threats for Micro, Small and Medium Enterprises (MSMEs) in East Java Province. The first opportunity is product standardization because with the provisions regarding standards, local products can find new ways to improve the quality of their products as well as being recognized as products that are suitable for sale in the international market. The second opportunity is market access. MSMEs will be able to easily sell their products to other ASEAN member countries. Meanwhile, the biggest threat to the AEC is product similarity because the elimination of tariffs has made imported products that are like local products can be sold at the same price or even cheaper. Nonetheless, both these opportunities and threats do not have a significant impact on MSME trade in East Java because they mostly sell their products to the domestic market.

# RECOMMENDATION

The results of these findings can be a reference for the Indonesian government, especially the province and cities in East Java to see the extent of the impact caused by the AEC after being implemented for approximately 5 years. With the findings showing that MSMEs in East Java are more oriented towards the domestic market than the international market, a new strategy is needed from the government so that the targets of these MSMEs are at least balanced between the domestic market and the international market. On the other hand, the use of local products also needs to be intensified again to minimize the threats that can be given by the AEC. The data used in this research is only limited to 2021 and does not fully cover all cities in East Java. By looking at the dynamics of the AEC in the years following 2021, future researchers may find different results considering that the number and actors of MSME exports in East Java can also increase or decrease.

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