

# CHAPTER I

## INTRODUCTION

### 1.1. Background of Research

China which currently emphasizes on economic development continues to develop product marketing strategies to other countries in various ways. By utilizing the various opportunities that are present, the Chinese government still persists in the existing cycle and trade regulation. This happens because of the state of mutual interests. The arrangement of countries in the world that underlies the bilateral and multilateral cooperation in the regional and international regions makes the foreign policy of each country change periodically. The arrangement also triggers an agreement in trading which required the existence of binding regulations in the form of export-import activities, payment methods in transactions, and other regulations.<sup>1</sup>

Countries which decide to approve trade agreements have new challenges in increasing domestic production to compete in trades that tend to be competitive. Therefore, policymakers must be more careful and vigilant towards trade partner country to survive the tight international trade. Determining foreign policy is a difficult thing to do in international cooperation. This occurs due to globalization and the development of issues which sometimes changed over time.<sup>2</sup>

Changes in a country's policies caused by economic interests are part of the international political economy. The actors determining economic policy are *power* and the country itself, two important things that are

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<sup>1</sup> Permata Siwi, "Bilateral Free Trade: Hubungan Perdagangan Indonesia-China dalam Kerangka ACFTA", *Journal Airlangga University*. Page: 3

<sup>2</sup> Thomas Outley, "International Political Economy Fifth Edition", *Routledge Taylor And Francis Group*, vol. 5 (2015). Page: 1

examined in international relations. In the international political economy, international cooperation was put forward by the liberal camp as a means to create peace.<sup>3</sup> In other words, international trade involving countries in cooperating tends to force the country to give and ask for their individual needs. Interactions in international trade can encourage the creation of good relations between countries positively.

The international agreement approved by the Association of Southeast Asian Nations with China in the ACFTA (*ASEAN-China Free Trade Area*) on January 1, 2010, is one example of good cooperation in international trade. Since the agreement was approved, the ACFTA had gained many awards, including *expansion of bilateral trade, expansion of bilateral foreign direct investment, additional progress in ACFTA related agreements, enhancement of regional integration* and also *strengtheness the understanding of ASEAN markets*.<sup>4</sup> Due to this award, the existence of the ACFTA agreement agreed to by the countries involved has been reached. The ASEAN-China Free Trade Area has more convincing advantages compared to other cooperation agreements between Indonesia and China. This is because the ACFTA discusses the issue of reducing tariffs, direct foreign investment, and regional harmonization. This issue was not discussed significantly in the bilateral agreement between Indonesia and China because in bilateral agreements Indonesia and China only discussed specific matters such as cooperation on maritime affairs, development, or the military.

The existence of the ACFTA forced its member countries to open markets to each other. Although Chinese products tend to be superior to other countries (this is driven by cheap price factors with high specifications

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<sup>3</sup> Mokhtar Mas'ood, *Ekonomi Politik Internasional dan Pembangunan* (Yogyakarta: Pustaka Pelajar, 2014). Page: 41

<sup>4</sup> Keith E. Flick and Kalyan M. Kemburi, *FREE TRADE AREA - Challenges, Opportunities and Threats*. Page: 11

provided by China), relations between countries in the region are still relatively good. Disputes or conflicts that occur in free trade are always completed quickly.

With the ACFTA, Indonesia as an ASEAN member country participates in the free trade cycle. As a consequence of the approval of the ACFTA, the Indonesian market has been filled with products from China with reduced import tariffs. Profits from the ACFTA agreement can be seen from the reduction in import tariffs from 12.8 percent to 0.6 percent.<sup>5</sup> Even though Indonesia-China relations have been established for a long time, the agreement on free trade has shown rapid development in export and import activities. These activities are driven by the productivity of multinational companies located in countries as controlled the target market.

In 2006 China's gains in the ACFTA reached \$ 139.96 billion USD and \$ 192.67 billion USD in 2008.<sup>6</sup> These results indicate that China's interests in improving the economy are successful and have a positive impact on the countries involved. Although the level of profit has proven to be high nominal, the continuity of cooperation in free trade must be maintained to ensure harmonization between countries in the agreement.

To master the international market, multinational companies must be able to increase productivity by utilizing the right technology, large-scale capital, and relevant sources. This is very important for multinational companies because the key to success in expanding can be seen from international competitiveness. In other words, aside from the gains made by multinational companies, international competitiveness is an absolute thing that can guarantee the continuity of companies operating on an international scale.<sup>7</sup> As an example of the fall of multinational companies that are unable to compete in the international market is Nokia Corporation. Based on the case

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<sup>5</sup> *Ibid.* Page: 28

<sup>6</sup> *Ibid.* Page: 29

<sup>7</sup> Sugeng Bob, *Politik Bisnis Internasional* (Yogyakarta: Kanisius, 2002).  
Page: 121

of Nokia Corporation, it can be seen that the continuity of a multinational company depends on competitiveness. In addition, the role of the state in encouraging the development of multinational companies is a supporting factor so that multinational companies can maintain competitiveness.

Xiaomi is an MNCs from China that experienced the fastest increase compared to other smartphone companies. This increase is based on innovation and different marketing strategies compared to other companies. One of the unique strategies applied by Xiaomi is to reduce the cost of advertising and use it to improve product quality so that it can be sold at a low price. This trigger the writer to make Xiaomi as the object of research, not other Chinese smartphone companies. Smartphone companies in general, innovate on the quality of products produced. This innovation was also carried out by Xiaomi as the nature of an MNCs.

In writing this research, the author will consider various conditions and views related to the discussion. In addition to the concepts and theories used by the author, this research will compare based on the views of Islam. This will prove the effectiveness of the use of concepts in research. With the comparison, it will be easier for the author to measure what supporting factors and the obstacles are.

The author deliberately choses the Islamic view as one of the things that can be compared with this study for several reasons. Islam is a comprehensive religion, which addresses almost all aspects of human life. This is in accordance with the word of Allah SWT as follows:

إِنَّ الدِّينَ عِنْدَ اللَّهِ الْإِسْلَامُ ۗ وَمَا اخْتَلَفَ الَّذِينَ أُوتُوا الْكِتَابَ إِلَّا مِنْ بَعْدِ مَا جَاءَهُمُ  
الْعِلْمُ بَعْيًا بَيْنَهُمْ ۗ وَمَنْ يَكْفُرْ بِآيَاتِ اللَّهِ فَإِنَّ اللَّهَ سَرِيعُ الْحِسَابِ

Means: “Indeed the religion (which is blessed) by Allah is only Islam. There is no quarrel among those who have been given the Book except after knowledge comes to them, because of envy (that is) between them. He who disbelieves in the verses of Allah, Allah is

fast in a reckoning”.<sup>8</sup>

By defining Islamic views as a comparison of research that is relevant to human life. The following is a verse of the Qur’an dealing with trade, and it also ideal in accordance with legal norms in life:

يَا أَيُّهَا الَّذِينَ آمَنُوا هَلْ أَدُلُّكُمْ عَلَىٰ تِجَارَةٍ تُنْجِيكُمْ مِنْ عَذَابٍ أَلِيمٍ. تَوَّابُونَ بِاللَّهِ  
وَرَسُولِهِ وَتُجَاهِدُونَ فِي سَبِيلِ اللَّهِ بِأَمْوَالِكُمْ وَأَنْفُسِكُمْ ذَلِكَُمْ خَيْرٌ لَّكُمْ إِنْ كُنْتُمْ  
تَعْلَمُونَ

Means: “O you who have believed, shall I guide you to a transaction that will save you from a painful punishment? (It is that) you believe in Allah and His Messenger and strive in the cause of Allah with your wealth and your lives. That is best for you, if you should know”.<sup>9</sup>

The paragraph mentioned above explains how to run a good and ideal trade. According to the Islamic view, even the smallest aspect is important and it must be done as well as possible. For this reason, the authors includes this relevant arguments in this study can be as a tool to analyze the objects discussed.

To further analysis how the role of the state in providing support to multinational companies needs special reviews based on relevant scientific theories and concepts. This paper, will discuss how the role of the Chinese government for multinational companies in expanding to the member countries of the *ASEAN-China Free Trade Area (ACFTA)*, especially in the case of Chinese businesses to help the expansion of Xiaomi Inc. in Indonesia.

## 1.2. Problem Formulation

Based on the development of international cooperation in economic

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<sup>8</sup> *Al-Qur’an: Al-Imran 19.*

<sup>9</sup> *Al-Qur’an: As-Shaaf 10-11.*

interests, the ASEAN-China Free Trade Area (ACFTA) agreement encouraged many multinational companies to expand as widely as possible in the region. Therefore, the author determines the formulation of the problem as a statement.

“How is the strategy of the Chinese government in exploiting the opportunities for ACFTA cooperation to encourage the expansion of multinational companies (Xiaomi Inc.) to the Indonesian market?”

### **1.3. Conceptual Framework**

To examine the attitudes determined by multinational companies, it is necessary to have relevant theories and concepts to examine the study. Therefore, the author uses liberal theory in international political economy.

#### **1.3.1. The Concept of Economic Liberalization**

In liberal economic theory, Mohtar Mas' oed stated the argument that the most effective way to increase national wealth is to allow individual exchanges in the domestic and international economy to run freely and unrestricted.<sup>10</sup> In another word, this theory advocates free markets as a means of increasing wealth.

In a liberal economy, there is an assumption that individuals (i.e. consumers, companies, or individual entrepreneurs) are the main actors who behave rationally and always strive to increase acquisition. Rational behavior itself is based on profit and loss calculations derived from various possibilities. If the actor has chosen a business that results in a high level of subject satisfaction, then the actor is considered to have the maximized acquisition.

In this study, liberal economic theory was used to explain how China's behavior faced the cooperation of ACFTA. As one of the countries that has a high income, China cannot be separated from its trading partners which have been the key for China in marketing the

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<sup>10</sup> M. Masoed, *Ekonomi-politik internasional dan pembangunan* (Pustaka Pelajar, 1994).

country's products. Therefore, a liberal economy that encourages free trade is a relevant theory used in this study.

### **1.3.2. The Concept of Multinational Enterprises (MNCs)**

To study this research further, it is not enough just to use the concept of international political economy. Therefore, the author uses the concept from another view as a tool to examine this research, namely the concept of multinational companies.

Since the end of World War II, the phenomenon of the International Politics noted a new development marked by the emergence of non-state actors who played their part in cross-national economic relations. One of the most prominent non-state actors in the context of international business is multinational companies (MNCs). With the power of capital, technology, and a good management system, MNCs control the flow of capital, technology, and even the distribution of goods across national borders.

The definition of multinational companies as quoted by Colman and Nixon by Bob Sugeng Hadiwinata in the book "*Politics of International Business*", namely multinational companies are business units that own or control assets such as factories, mining, plantations, outlets (shopping centers) and offices that in two or more countries.<sup>11</sup>

While the role of multinational companies according to Robert Gilpin in the book "*US Power The Multinational Corporation*", are as follows:<sup>12</sup> "The role of the company can, open new employment opportunities, improve capabilities or abilities, help develop technology, and expand international markets".

Foreign direct investment is a potential source of foreign financing compared to other sources because the source of foreign capital inflow

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<sup>11</sup> Bob, *Politik Bisnis International*. Page: 117

<sup>12</sup> R. Gilpin, *U.S. Power and the Multinational Corporation: The Political Economy of Foreign Direct Investment* (Basic Books, 1975). Accessed 17 Oct 2018

is mostly in developing countries due to the gap of capital. The capital gap occurs due to technological developments, reduction or restrictions for foreign investment and acquisitions, as well as deregulation and privatization in various industries, Claessensini's view in accordance with Hausman and Arias's<sup>13</sup> opinion that foreign direct investment is a subsidiary of capital market development, because the entry of foreign direct investment can overcome investment difficulties through the capital market, given that shareholders' rights are not protected.

Another view is that foreign direct investment in countries with good fundamentals can help develop the domestic financial system. Foreign direct investment can be a driver for the development of the stock market, namely through the capital market and participating with companies, because foreign investors may want to fund part of their investment with external capital or also want to invest again by selling shares in the capital market. Second, given that some foreign investors invest through equity purchases. This investment is carried out by companies or entities that exist in one country or become companies or entities in other countries. Foreign direct investment differs substantially from indirect investments such as portfolio flows, where overseas institutions invest in equity registered in a stock exchange. Entities making direct investments usually have a significant degree of influence and control over the company where the investment is made.

In this study, the concept of multinational companies is used to analyze how non-state actors can take a role in International Politics. The behavior is shown by most multinational companies that expand as widely as possible to get more profits. In this study, the Chinese government took advantage of opportunities from the ACFTA collaboration that facilitated the flow of goods and products, and

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<sup>13</sup> Hausmann and Fernandez-Arias, "Foreign Direct Investment : Good Cholesterol ? The New Wave of Capital Inflows : Sea Change or Just Another Tide ?", *Development* (2000).

investment. By reducing the prices of goods or products to be cheaper, multinational companies which compete with the domestic market can survive better than multinational companies selling trademarks.

## **1.4. Purposes and Benefits**

### **1.4.1. Research Purposes**

Based on the background above, this study aims at finding out more deeply about Chinese policies in encouraging Xiaomi Inc. as a multinational company to expand into the territory of Indonesia with the encouragement of the international cooperation factor *ASEAN-China Free Trade Area* (ACFTA) and its interests in carrying out such expansion. Whereas specifically, this study aims at:

1. Knowing why China chooses Indonesia to be the market target of the multinational company's product.
2. Answering the formulation of the problem with relevant to theories and concepts and proving the truth of the hypothesis with facts and data.

### **1.4.2 Research Benefit**

This research is expected as follows:

1. Academically as a means of understanding the concept of international companies in free trade.
2. Practically to find out more about the things that are driving Chinese policy towards a multinational company, especially in expanding its products to countries in Asia.

## **1.5. Review of Related Literature**

Impacts of the *ASEAN-China Free Trade Area* (ACFTA) have previously been widely discussed and examined by several researchers. It's just not specific to the research on the behavior of multinational companies that are also important actors in this free trade. Therefore, there is a need for further research related to the study of multinational companies that take a

large role in the cooperation of ACFTA.

The researches of several researchers discussing the cooperation of ACFTA and its impact have been presented in scientific works such as the writings owned:

The first author described the development of Chinese textile products in Indonesia after the implementation of ACFTA. This type of research used descriptive, which described the analysis of the Indonesian government's policy in dealing with ACFTA which had an impact on the marketing of Chinese textile products in Indonesia. The data presented were based on secondary data through literature studies such as books, internet, and others. The analysis technique used was the analysis of qualitative techniques. The results of the study showed that free trade cooperation between Indonesia and China within the framework of the ACFTA had an influence on the trade in textile products. Chinese textile products traded in Indonesia were cheaper than domestic products, so China obtained more profits.<sup>14</sup>

The second author tried to explain how bad the impact of the ACFTA cooperation was for the domestic market which was unable to compete with Chinese products. The Indonesian government were considered as serious pressure on relatively weak domestic businesses compared to products produced by the Chinese state. The pressure on the cooperation of the ACFTA should be able to be an encouragement for Indonesia to continue was develop, and improve the quality of the domestic products produced, so it is able to compete with Chinese products in the domestic market.<sup>15</sup> Therefore, the author analyzed the extent of the impact of the ACFTA and how the process should be carried out so that the expectations expected from the ACFTA collaboration had a positive impact on Indonesia.

The third author, in his research on the *ASEAN-China Free Trade*

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<sup>14</sup> Iswandari, *PERKEMBANGAN PRODUK TEKSTIL CINA DI INDONESIA PASCA IMPLEMENTASI ACFTA ( ASEAN-CHINA FREE*, vol. 2010 (2014), p. 2014.

<sup>15</sup> Lidya Christin Sinaga, *INDONESIA DI TENGAH KESEPAKATAN ACFTA (1997)*.

*Area* (ACFTA), explained how China could compete in free trade which tended to be competitively lifted from textile products. In the application of free trade, China was trying to reduce prices as low as possible so that its products could match domestic textile products. After China's strategy in free trade had been classified in general in research, this has become an important variable for researchers to know the extent to which Chinese products could compete.<sup>16</sup> The strategy used by China in free trade was to find what was not available in the target market, then what products could be sold in the market, and what products are current trend. Besides knowing how much capacity the goods can be sold in the free market was the most important variable in China's sales strategy in free trade.

The fourth author wrote research on the impact assessment of the *ASEAN-China Free Trade Area* (ACFTA) goods trade agreement for Indonesia and China. The quantitative approach with the econometric analysis was used to assess the influence of the ACFTA on both parties in terms of export and growth contributions. The results of the study indicated that Indonesia had not utilized the ACFTA scheme optimally so that it had less benefits than China. As a result of participating in the ACFTA, Indonesia's exports to China increased by the US \$ 116 million per year or 5.83% per year. While China's exports to Indonesia amounted to the US \$ 5.6 billion per year or 18.55% per year. For this reason, Indonesia had to strive more aggressively balance China, among others, through bilateral agreements, mastery of China's national standards, minimizing the impact of sectoral adjustments in the five most affected sectors and optimizing use of *anti-dumping* policies.<sup>17</sup>

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<sup>16</sup> Rudi Hartono, "PENGARUH KERJASAMA ASEAN-CHINA FREE TRADE AGREEMENT (ACFTA) TERHADAP PASAR DOMESTIK PRODUK TEKSTIL INDONESIA", *Program, Mahasiswa Internasional, Ilmu Hubungan Sosial, Fakultas Ilmu Politik, Ilmu Mulawarman, Universitas*, vol. 1, no. 4 (2013), pp. 1077–84. Page: 1

<sup>17</sup> Sigit Setiawan, "Asean-China Fta : Dampaknya Terhadap Ekspor Indonesia Dan Cina", *Buletin Ilmiah Litbang Perdagangan*, vol. 6, no. 2 (2012), pp. 1–27.

## **1.6. Research Methodology**

The research method is the process used or taken by the author in a study. Research is a systematic process that is carried out to increase knowledge and also efforts made to find an answer to the problem. The emergence of problems in a study requires the existence of good relevant methods to solve problems in the right way.

The use of methods in each study is different, depending on the problem and the factors which motivate researchers to solve the problem under study. To facilitate the author in completing this research, the research methods used will be described as follows:

### **1.6.1. Research Method**

The type of research used by the author is library research or literature research methods. According to Noeng Muhajir, library research requires more philosophical and theoretical processing than empirical tests in the field.<sup>18</sup> Because of its theoretical and philosophical nature, this type of research tends to use a philosophical approach compared to other approaches. The method is supported by data sources, data collection, and data analysis.

### **1.6.2. Research Objects**

To obtain the materials needed in this study, various literature related to the cooperation of ACFTA, Chinese economic policy, and expansion of multinational companies in the form of references or reports on other research results relevant to this research will be used as objects in research.

### **1.6.3. Technique of Data Collection**

The technique used by the author in this study uses the

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<sup>18</sup> H.N. Muhadjir, *Metodologi penelitian kualitatif: pendekatan positivistik, rasionalistik, fenomenologik, dan realisme metaphistik, telaah studi teks dan penelitian agama* (Rake Sarasin, 1996), <https://books.google.co.id/books?id=3oXwAAAACAAJ>. Accessed 17 Dec 2018.

documentation method, to look for data on things or variables in the form of articles in newspapers, books, journals, statistical data, reports, organizational records, government publications, results of previous surveys, pre-made analysis, records of official events and notes in the library.

In the context of this research, the author collects main and supporting data and holds a *check-list* to look for predetermined variables from the literature, other researches, journals and published reports, especially related to China's foreign policy in the economy and free trade, and also its interests in expanding into Indonesia, so that it is expected to answer the objectives of the research problem.

### **1.7. Thesis Statement**

Based on the formulation of the problem and background which have been written by the previous author and associated with theories and concepts that are relevant to the discussion, the author concludes that:

1. China's strategy in utilizing ACFTA opportunities is to expand in the Southeast Asia region. Reducing barriers and decreasing export tariffs are good opportunities for China to take greater profits.
2. Xiaomi provides high-quality products and low prices as an unusual strategy. This method is Xiaomi's strategy to beat other smartphone products.

### **1.8. Systematic Discussion**

#### **BAB I : INTRODUCTION**

In this section, the author will explain the background of the problem, the formulation of research problems, the framework of thinking, research methods and systematic discussion. In general, this section will explain the description of the problem so that the author can determine the hypothesis as a temporary answer. This section also explains about the systematic discussion to find out the discussion explained in the next section.

#### **BAB II : ASEAN-CHINA FREE TRADE AREA (ACFTA) AND**

## ACTORS ASSOCIATED IN THE AGREEMENT

This section will point out how the ACFTA collaborates and the actors involved in the economic agreement. The collaboration dealing with free trade gives a certain influence and discusses issues that become obstacles in free trade. While the actors involved have an active role to determine the development of this collaboration so that the interests of each can be achieved. Actors who play a role here are member countries of ASEAN, China, and multinational companies (MNCs).

## BAB III : THE STRATEGY OF CHINA THROUGH XIAOMI'S EXPANSION TO DEAL WITH TRADE WAR

This section will explain the expansion of Chinese multinational companies in Indonesia based on certain interests. For this reason, this section will explain how the behavior of multinational companies and what factors trigger multinational companies is to expand to other countries. In this section, the author also describes several opportunities that are indicators for companies to take advantage of international cooperation and explain the comparison of theories with Islamic views.

## BAB IV : CLOSING

This section is the closing as well as an explanation of the conclusions of the research discussed in the previous section. In general, in this section the author will draw conclusions, suggestions, and answers to the previous hypothesis.