

## **Indonesia's Opportunities and Challenges in IK-CEPA: Bilateral Free Trade Agreement with South Korea**

**Salismi Zulfi Maulidita**

Korean Language Program, Sejong Korean Academy of Yogyakarta, Indonesia

E-mail: szulfimauidita@gmail.com

**Darmanto**

Liberal Arts Department, Sehan University, South Korea

E-mail: darma3388@gmail.com

### **Abstract**

The IK-CEPA was officially implemented in 2023 as a commitment between Indonesia and South Korea to cooperate in marketing and fulfil commodity needs, aiming for better and more sustainable economic development. This paper seeks to investigate the opportunities and challenges faced by Indonesia in implementing the IK-CEPA. The comparative method is applied to analyze the secondary data sourced from official publications on bilateral agreements between the two countries, and statistical data on investment, trade, and the country's trade balance. A comparative data analysis was conducted by comparing the IK-CEPA with the previously implemented free trade agreement (FTA) in Indonesia with similar values, namely the IA-CEPA. In this paper, the IA-CEPA serves as a crucial point of comparison from which analytical results concerning the potential opportunities or challenges of the IK-CEPA were derived, focusing on several indicators like foreign direct investment (FDI) flow, trade value, and trade balance. The results show that Indonesia has the opportunity to: (1) increase the FDI value; (2) increase trade values with South Korea; and (3) improve the trade balance with South Korea to achieve a surplus. Two challenges for Indonesia in this endeavor include failure to achieve a trade balance surplus and the need for maximum utilization of the IK-CEPA by the Micro, Small and Medium Enterprises (MSMEs).

**Keywords:** bilateral cooperation, comparative analysis, free trade agreement, IK-CEPA

### **Abstrak**

*IK-CEPA resmi dilaksanakan pada tahun 2023 sebagai komitmen Indonesia dan Korea Selatan untuk bekerja sama dalam pemasaran dan pemenuhan kebutuhan komoditas, guna mencapai pembangunan ekonomi yang lebih baik dan berkelanjutan. Tulisan ini berupaya menyelidiki peluang dan tantangan bagi Indonesia dalam mengimplementasikan IK-CEPA. Metode komparatif diterapkan untuk menganalisis data-data yang telah dikumpulkan dari sumber sekunder seperti publikasi resmi mengenai perjanjian bilateral antara kedua negara, dan data statistik mengenai investasi, perdagangan, dan neraca perdagangan suatu negara. Analisis data komparatif dilakukan dengan membandingkan IK-CEPA dengan bentuk perjanjian perdagangan bebas (FTA) yang serupa dan pernah diterapkan Indonesia sebelumnya, yaitu IA-CEPA. Dalam tulisan ini, IA-CEPA berfungsi sebagai titik perbandingan penting untuk memperoleh hasil analisis mengenai potensi peluang atau tantangan IK-CEPA, dengan fokus pada beberapa indikator, yaitu aliran penanaman modal asing (FDI), nilai perdagangan, dan neraca perdagangan. Penelitian ini menemukan bahwa Indonesia mempunyai peluang untuk: (1) Meningkatkan nilai FDI; (2) Meningkatkan nilai perdagangan dengan Korea Selatan; dan (3) Memperbaiki neraca perdagangan dengan Korea Selatan hingga mencapai surplus. Selain itu, hasil penelitian*

*ini menyoroti dua tantangan bagi Indonesia: (1) Kegagalan mencapai surplus neraca perdagangan; dan (2) Perlunya pemanfaatan IK-CEPA secara maksimal oleh Usaha Mikro, Kecil, dan Menengah (UMKM).*

**Kata kunci:** *IK-CEPA, kerja sama bilateral, metode komparatif, perjanjian perdagangan bebas,*

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## INTRODUCTION

The Indonesia-Korea Comprehensive Economic Partnership Agreement (hereafter, IK-CEPA) was launched by President Susilo Bambang Yudhoyono and President Lee Myung Bak in 2012, which started a series of comprehensive negotiation processes (Santoso, 2022; Septana, 2017; Umaira, 2022). Negotiations between Indonesia and South Korea in the IK-CEPA have been highly dynamic and, to date, are subjected to certain studies. However, most IK-CEPA research discuss the implications and negotiation process for the IK-CEPA ahead of its final implementation in January 2023 (Tiara, 2017; Ismail & Mulyaman, 2018; Bila & Wijayati, 2022; Cholif & Paksi, 2022; Safitri, 2021). This research continues the discussion of pre-existing studies, elaborating Indonesia's opportunities and challenges in implementing the agreement by comparing it to a previous bilateral agreement between Indonesia and Australia (IA-CEPA). Referring to the Work Report of the Directorate General of Law and International Treaties Ministry of Foreign Affairs of Indonesia in 2019, the IK-CEPA has been supported based on the same multilateral agreements or negotiations like the ASEAN-Korea FTA agreement/investment agreement and RCEP, and bilateral agreement such as IA-CEPA (Ministry of Foreign Affairs RI, 2021).

South Korea is a strategic trading partner for Indonesia. Since 1973, the two countries have fostered diplomatic

relations and preserved cooperation in political, economic, cultural, and other fields. Indonesia's export values to South Korea grew 38% in 2021 to US\$8.98 billion while the imported goods increased by 37.63% to \$9.42 billion (Databoks, 2022). In addition to abundant natural and human resources, Indonesia has accelerated progress in the manufacturing and service sectors. South Korea, on the other hand, has achieved remarkable economic development in industry, technology, and skilled labor management. As trade and investment ties in recent years has expanded rapidly at a global scale, sharing resources between the two countries potentially brings enormous advantages.

The IK-CEPA coordinates trade in goods, services, investment, economic, legal, and institutional cooperations between Indonesia and Korea. After its initiation in 2014, IK-CEPA negotiation was suspended for three years due to failure to arrive at mutual agreement. Nevertheless, the COVID-19 pandemic outbreak that brought significant changes across the globe prompted the IK-CEPA to be consensually reactivated in 2019. The transition of presidents in both countries also contributed to this reactivation (Safitri, 2021).

Cooperation is formed due to arising diverse problems at national, regional, or global levels that require the involved countries to immerse (Holsti, 1983). In line with Holsti, other scholars taking liberalism perspective posit that cooperation is a wise option where

countries can join forces to overcome problems and achieve common interests (Falk, 2002; Moravcsik, 1993; Reinsberg, 2021). One manifestation of bilateral and multilateral cooperation emphasized by Indonesia is economic affairs (Damuri & Friawan, 2022; Jose & Samudra, 2022; Yani & Nizmi, 2018), especially cooperation through FTAs (Adam & Negara, 2017; Nugraha, 2019; Ragimun et al., 2022; Rissy, 2021).

Adhering to the commitment to realizing public welfare as a national constitution, the economic sector emerges as a vital sector in *Nawacita* or nine work priorities stipulated by President of the Republic of Indonesia. Initiated by Joko Widodo and Jusuf Kala, *Nawacita* promotes have nine purposes: (1) resisting a weak country by implementing system reform and law enforcement that is corruption-free, dignified, and trusted; (2) building Indonesia from the outskirts by strengthening regionals and villages within the framework of the unitary state; (3) fostering diversity and strengthening Indonesian social restoration; (4) ensuring the country protects and provides a sense of security to all of its citizens; (5) realizing active governance by building a government that is clean, effective, democratic, and trustworthy; (6) improving the quality of life of Indonesian people; (7) realizing economic independence by mobilizing strategic sectors of the domestic economy; (8) conducting a national character revolution; and (9) improving people's productivity and competitiveness in the international market. To boost economic development, Indonesia has explicitly set an annual economic growth target of 6.0% per year on average in 2020–2024, a one-fifth

increase from 5.0% in 2015–2019 (BAPPENAS, 2020). Hence, even in Indonesian foreign politics, the economic sector is one of the diplomacy objectives in the Indonesia Ministry of Foreign Affairs priorities, and the emphasis is continuously pursued.

While previous research mainly discussed the early implementation of IK-CEPA cooperation, the present paper probes deeper into opportunities and challenges of IK-CEPA through a comparative analysis between the IK-CEPA and similar bilateral economic agreements in Indonesia. Launched in January 2023, IK-CEPA is currently at the infancy stage with plenty rooms for discussion on opportunities and challenges of the IK-CEPA to explore the potential possibilities for Indonesia and South Korea. This study expects to serve as a practical reference point for stakeholders in viewing the challenges to anticipate and possibilities to maximize through the IK-CEPA collaboration. Scholars interested in understanding the evolving landscape of Indonesia–Korea bilateral relations, especially in terms of economy can find this paper insightful.

## **Conceptual Framework**

### *Free Trade Agreement*

In general, countries implement three types of trade agreements based on the number of countries involved. These are (1) trade agreements by a country that imposes trade limitations, known as unilateral trade agreements; (2) agreements that bind two countries to loosen trade restrictions and expand business opportunities, known as bilateral agreements; and (3) trade agreements that bind more than two countries and are an agreement with the most complicated negotiation process,

known as multilateral agreements (Amadeo, 2021). As soon as the agreement crosses the regional level, the World Trade Organization will intervene to assist the countries in implementing negotiations and enforcing trade agreements.

Conversely, the free trade agreement (FTA)—the opposite of protectionism and economic isolationism—is the propensity to buy and sell goods and services across borders without government interference in terms of tariffs, quotas, subsidies, or prohibitions (Barone, 2022). The countries often agree on formal and mutual agreements that balance commitments. Bilateral FTAs were first signed in the 1970s and widely adopted in the 1990s and 2000s. The country that establishes free trade policies and agreements does not inescapably relinquish all controls over imports and exports or eliminate every single protectionist economic measure. Only a few agreements offer complete free trade. It was reported that exports between countries engaged in bilateral FTA accounted for only 0.6% of world exports (ILO, 2015).

FTAs resemble joint trade cooperation between nations in many ways, except for their focus on producing and trading resource goods derived from the origin country. One distinct feature is the imported commodities to meet domestic demands, that also include intellectual property rights, rules on digital trade, and other standard settings (Sinha, 2022). These more profound agreements will likely have significant economic impacts on member states, but also negative impacts on some sectors and demographics (Cali et al., 2019). A side effect of FTA is that it complexifies customs structures, leading to

inefficiencies in resource allocation. Standards tariff that overlaps with FTA tariff concessions and some rules of origin (RoO) adhered to FTAs has undermined the customs system's efficiency and creates room for corruption (Athukorala, 2020).

Given the wide range of potential side effects associated with an FTA, the consideration of possible opportunities and challenges is absolutely necessary. In this case, referring to several studies that discuss the opportunities and challenges of FTAs (Ethevenin, 2018; Istifadah, 2012; Lee & Okabe, 2011), the value of such opportunities and challenges can be analyzed by conducting assessments to several aspects, namely: (1) contents of the agreement, such as the tariff policy that will be enforced, RoOs, and preferential origin; (2) policy discourse that will be implemented; and (3) coordination of the two previous points with the country's current conditions, i.e., economic conditions, market access, export potential, investment flow, and competitive pressure.

## **Research Methods**

This study employed a qualitative approach with a comparative analysis method. Referring to Shank (2002), qualitative research is empirically based on experience, and researchers seek to understand how others make sense of the phenomenon being investigated. Focusing on multiple methods, qualitative research generally takes an interpretive and naturalistic approach (Aspers & Corte, 2019) or a comparative approach (also referred to as qualitative comparative analysis) which, the first version, was created by Charles Ragin as an analytical technique in the 1970s.

As indicated in the previous subchapter, evaluating various aspects of FTAs enables researchers to study their opportunities and challenges. This paper summarized the aspects of FTAs required for analysis—contents and policies of the agreement, and current situations—into three main indicators, which were then compared. These indicators are (1) the current condition of FDI value between Indonesia and Korea; (2) the current condition of trade value; and (3) the current condition of trade balance. Therefore, the FTA aspects were assessed as part of a systematic evaluation process to understand the potential opportunities and challenges of the IK-CEPA by comparing them with those of another bilateral FTA, IA-CEPA. It should be noted that both the IK-CEPA and IA-CEPA exhibit similar trade cooperation values and regulate investment deals.

Comparative research allows information gathering to demonstrate the limitations or effectiveness of a policy (Stone, 2001). In this study, the IA-CEPA serves as a crucial point of comparison for obtaining analytical results regarding the potential opportunities or challenges of the IK-CEPA. Such comparisons are valuable for bolstering research outcomes and providing comparison factors that validate the significance of the research results. An emphasis on descriptive explanations and focus on concept formation through comparison analysis of the similarities and differences of a phenomenon or case is required for conducting a comparative analysis (Collier, 1993). This study used a documentation technique to gather data from secondary sources in the form of official publications on bilateral agreements between the two countries,

and statistical data on investment, trade, and the country's trade balance, studies, and other relevant literature.

## **DISCUSSION AND RESULTS**

### **Content and Objectives of the IK-CEPA**

Indonesia ratified the IK-CEPA in 2022 as a national regulation in Law Number 25 of 2022. IK-CEPA regulates all aspects of free trade that include reduction or elimination of tariff barriers, regulations of origin, custom procedures, trade in services and investment, trade facilitation, and trade remedies in economic and institutional cooperation. This set of regulation aims at maximizing the economic potentials of both countries by equitably and sustainably increasing the free movement of goods, services, investment flows, and skilled labor.

Regarding trade in goods, South Korea's commitment to the IK-CEPA is to liberalize 95.5% of the total postal rates through two stages. The first is Fast Track (EIF), which eliminates 0% of the 11,267 tariff barriers in South Korea (or 92% of the total goods tariff). The second stage is Gradual Elimination, which gradually eliminates 420 South Korean tariff barriers (or 3.4% of the total goods tariff) within 3–20 years after implementation (Fact-Sheet IK-CEPA, 2020). Goods tariff is eliminated from some Indonesian products such as lubricating base oil, stearic acid, clothing, blackboards, dried fruit, and seaweed (Fact-Sheet IK-CEPA, 2020). Indonesia also reduced 9,954 tariff barriers, or liberalized around 92.06% of the total tariff barrier on goods imported from South Korea. Eliminating tariff barrier headings to other countries means that Indonesian-produced goods, as per the RoOs, can be imported free of charge, and therefore, Indonesian goods can be delivered free of charge (0% of the

agreed value) to South Korea. Chapter 3 of the IK-CEPA Agreement states that the intended original products are those entirely produced and processed in the parties' territories, including (1) plants and products from plants grown and harvested in the parties' area; (2) animals born and raised in the land of parties and stocks produced from them; (3) goods obtained from being hunted or caught in the parties' territories; and (4) minerals and other naturally-occurring substances which have been extracted in the parties' territories (IK-CEPA Agreement Chapter 3, 2020).

As for trade in services, South Korea is committed to opening several service's sub-sectors with Foreign Equity Participation (FEP) up to 100%, such as construction and other related services, and audio-visual services (Fact-Sheet IK-CEPA, 2020). The agreement refers to buying shares or allowing partial ownership in exchange for financing the agreed service sectors. South Korea also agreed to liberalize some service sectors sooner or later, such as franchise sectors, construction, and computer-related services. While directly focused on service sector business, South Korea also supports the workforce quality improvement in service trade sector by accelerating the movement of intra-cooperate transfers, business visitors, and independent professionals (Fact-Sheet IK-CEPA, 2020).

Another form of cooperation stated in the IK-CEPA is South Korean investment to Indonesia in which both countries agreed to provide better investment facilitation regarding protection or market access for investors by applying the principle of "Most Favored Nation Treatment" and "National Treatment." Additionally,

protection is regulated in the investment sector, which includes non-discriminatory treatment for both countries, fair and equitable treatment, and investor dispute settlement.

In terms of economic cooperation, Indonesia and South Korea agreed upon specific agendas, including the industrial sector, agriculture, trade rules, procedures, person movements (MNP), and other cooperation sectors concerned with supporting MSME enterprises, infrastructure, investment, culture and creative fields, and health services. As written in Chapter 8 of the agreement, this cooperation takes the forms of (1) technical assistance; (2) training of human resources; (3) exchange of data and information; (4) exchange of experts; (5) thematic seminars or workshops; (6) design and improvement institutions; (7) formulation of the sectoral master plan; (8) formulation of development strategy; (9) sharing of best practices; (10) base studies; (11) joint research and development; (12) joint trade and investment, promotion activities; (13) model and technology transfer; and (14) other forms of cooperation as may be agreed by the parties (IK-CEPA Agreement Document Chapter 8, 2020).

### **Content and Objectives of the IA-CEPA**

The IA-CEPA is a bilateral FTA between Indonesia and Australia. Officially implemented on July 5, 2020 during the economic turmoil resulting from the COVID-19 pandemic, IA-CEPA was ratified in hope for advocating Indonesia's post-pandemic economic recovery. IA-CEPA aims to establish economic powerhouses in the region to significantly increase the influence, energy, and power of both countries in the region.

IA-CEPA agreement links three main aspects: market access, capacity building and trade cooperation, and investment. For trade cooperation, it has been settled to focus on trade in goods and services, and the elimination or reduction of goods tariff barriers up to 0% with a total of 6,474 tariff posts (Fact Sheet Indonesia-Australia CEPA, 2019) – two sectors stipulated in IK-CEPA. In the investment sector, the regulations include minimum standards and prohibitions; regulation of investors, individuals, and legal entities; and the application of the Most Favored Nation Treatment principle and the National Treatment Principle (Rissy, 2021). Other focus areas include economic cooperation and human resources. Regarding economic cooperation, the IA-CEPA facilitates a sustainable increase in trade by supporting and facilitating trade and investment, economic growth and prosperity, and the establishment of the Economic Cooperation Committee. For human resources, Australia facilitates improving Indonesian human resource quality at the international level through the IA-CEPA.

The difference between the IA-CEPA and IK-CEPA lies on the spirit. IA-CEPA hopes to lead to a mutual “Economic Powerhouse” in the region, fostering Indonesia-Australia collaboration between by harnessing each other’s advantages and productivity to target market access to the third countries. Meanwhile, the IK-CEPA was established for (1) achieving substantial value from the liberalization of trade in goods and services; (2) increasing investment value; (3) promoting fair economic competition; and (4) establishing a framework for effective and sustainable cooperation and capacity building for

development (IK-CEPA Agreement Document Chapter 7, 2020). Some of the principles held in the rules of origin (ROO) are similar, but have been adjusted to the needs of the respective party.

Comparatively, the IA-CEPA and IK-CEPA were drafted as border schemes of economic cooperation rather than agreements narrowly focused on trade cooperation. The formulation of the IK-CEPA refers to the basis points of several FTAs, including IA-CEPA. Hence, it is natural that some essential points in both agreements like the form of cooperation and the focus on the trade sector, investment, and economic cooperation, would facilitate human resource development. This shared concept can be used as an initial predictive view of the IK-CEPA which was implemented after the IA-CEPA by looking at the implications of the latter and determining the opportunities and challenges that might occur to Indonesia in implementing the former.

### **Indonesia’s Opportunities through the IK-CEPA: A Comparison with the IA-CEPA**

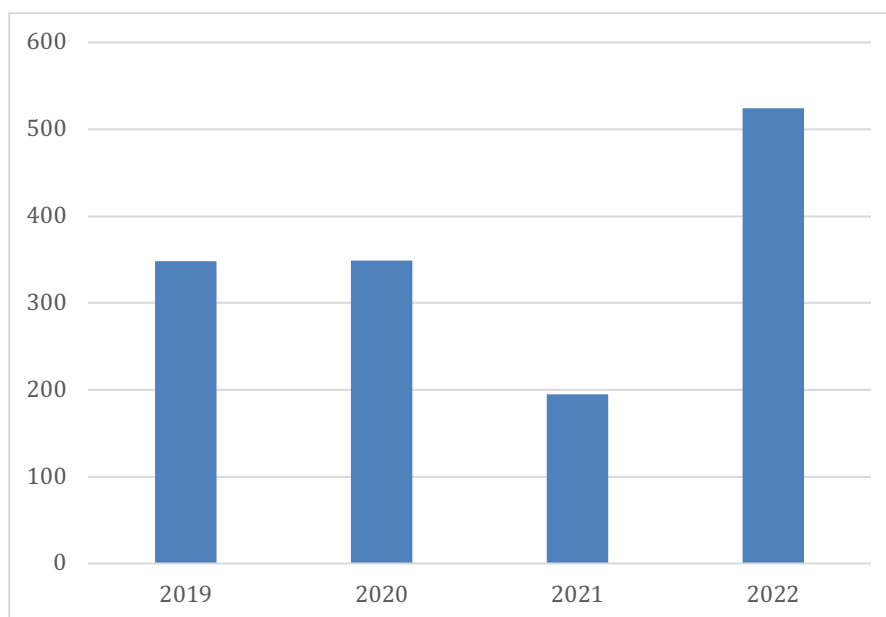
South Korea has become Indonesia’s preeminent economic partner (Ballbach, 2023; Dae-Chang, 2013; Indraswari, 2021; Poetri, Govindasamy, and Akhir, 2018). As a cooperation between Indonesia and South Korea, IK-CEPA proves a flourishing cooperative relationship for both countries. For Indonesia, the agreement brings excellent opportunities for increasing competitiveness and market access for Indonesian products and workers in Korea. In turn, IK-CEPA is a strategic booster for Korean investment in Indonesia and economic cooperation for both countries. The opportunities

afforded by the agreement are explored within this sub-chapter.

The first Indonesia's opportunity through the IK-CEPA is analyzed by comparing the current situation of FDI values between Indonesia, South Korea, and Australia. Subsequently, this study compared the investment sectors in IK-CEPA and IA-CEPA to assess future opportunities and challenges.

According to the Minister of Trade of the Republic of Indonesia, Muhammad

Lutfi, the enactment of the IA-CEPA is a righteous momentum in recovering Indonesia and Australia's post-pandemic economic problems (Indonesia, 2021). Based on the statistical data shared by the Indonesian Ministry of Investment through the National Single Window for Investment (NSWI), investment values in Australia increased in 2022 after a significant decline in the previous year (see Figure 1).



**Source:** Indonesian Ministry of Investment, 2023.

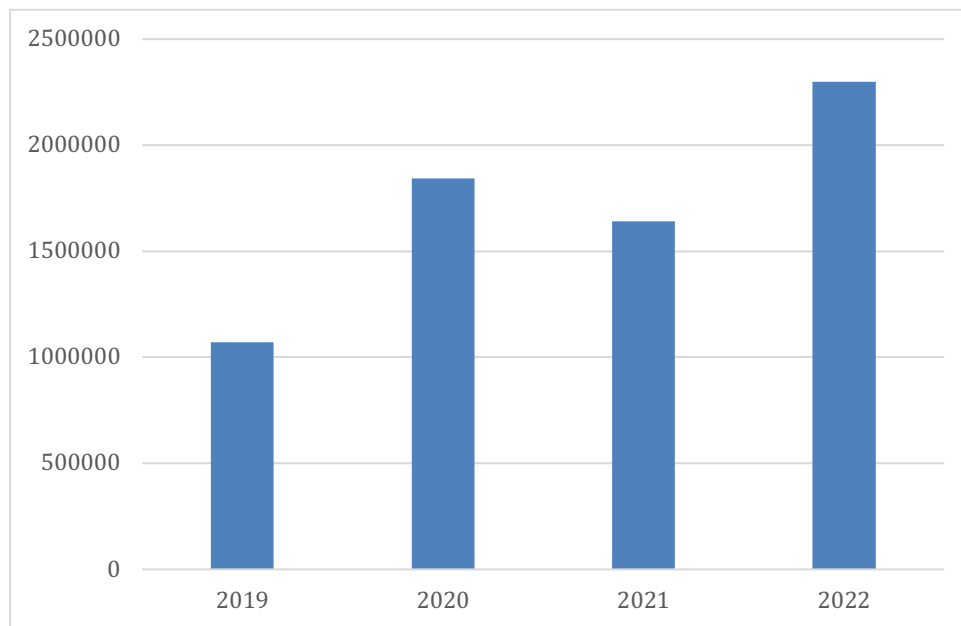
**Figure 1.**

Development of FDI Realization by Australia in 2019/2022

Figure 1 illustrates that in 2019, the actual value of Australia's FDI in Indonesia was US\$348,265.80 and increased slightly to US\$348,553.30 in 2020. One year after the enactment of IA-CEPA (2021), the investment value decreased to \$195,195.5, before it rose significantly to its peak of \$524,408.50

generated by a total of 982 investment projects in 2022.

Meanwhile, before the enactment of IK-CEPA, South Korea's investment value in Indonesia had reached US\$2,297,835.10 in 2022, marking the highest value recorded from 2019 to 2022 (see Figure 2).



Source: Indonesian Ministry of Investment, 2023.

**Figure 2.**

Development of FDI Realization by South Korea in 2019/2022

As per Figure 2, the value of South Korean investment in Indonesia has followed an upward trend. Between 2019 and 2020, the actual value of South Korean FDI in Indonesia increased from US\$1,070,212.50 to US\$1,841,946.30, then decreased slightly to US\$1,640,156.40 in 2021 due to challenges posed by the COVID-19 pandemic and global inflation. In other words, South Korean investments in Indonesia did not seem to be overly affected by such external factors as pandemics and inflation, and therefore, the IK-CEPA appears to be a promising opportunity for Indonesia. In 2022, there were 2,907 South Korean investment projects in Indonesia, and at least 3,071 projects by mid-2023 (NSWI BKPM, 2022). It was a notable disparity between Korean and Australian investment projects executed in Indonesia.

On the other hand, both IK-CEPA and IA-CEPA shared common characteristics

in investor sector; both agreements apply the Most Favoured Nation Treatment principle and the National Treatment principle to support increased investment flow. Each of these principles contains an agreement with similar essence, namely to provide fair treatment to every investor from both parties, which in this case, IK-CEPA and IA-CEPA agree not to include international dispute resolution procedures or mechanisms (Investor-State Dispute Settlement). These similarities show that both South Korea and Australia have an equal footing in treaty agreements. However, when considering the current conditions of FDI between Indonesia, South Korea, and Australia, it is evident that IK-CEPA presents greater opportunities in foreign direct investment flow compared to IA-CEPA.

The second opportunities brought by IK-CEPA to Indonesia are analyzed by comparing the current trade values

between Indonesia, South Korea, and Australia, as well as the trade deals of the IK-CEPA and IA-CEPA agreements in order to assess future opportunities and challenges in the trade sector.

During 2021, trade activities between Indonesia and Australia increased rapidly, recording US\$12.64 billion trade in goods (the highest since 1989) and a growth of 28.62% Indonesian export goods to Australia (year-on-year; YoY) to US\$3.22 billion (Rahman, 2022). In the same year, Indonesia’s trade in goods to South Korea increased by 37.8% from the previous

year to US\$18.4 billion to which, according to Databoks (2022), South Korea contributed 0.04% to Indonesia’s total trade value. Therefore, a positive opportunity to increase trade between the two countries through the IK-CEPA is evident, especially considering that growth of Indonesian goods exports to South Korea by 38% to US\$8.98 billion in 2021. In the same year, the import value from South Korea increased by 37.63% to US\$9.42 billion (Databoks, 2022).

Table 1 below compares the agreement between the IK-CEPA and IA-CEPA in the trade sector:

**Table 1.**  
The IK-CEPA and IA-CEPA in the Trade Sector

IK-CEPA	IA-CEPA
South Korea eliminated 95.5% of its tariff posts (a total of 11,000 of Indonesia products were free or 0 tariff points entering South Korea)	Australia eliminated 6,474 tariff posts (100% of the total tariff posts) to make all import duties on Indonesian products to Australia 0%
Indonesia will eliminate 92% of tariff posts.	Indonesia eliminated 10,229 tariff posts (94.5% of total tariff posts)

**Sources:** Free Trade Agreement Center, 2024; Free Trade Agreement Center, 2023; Free Trade Agreement Center, 2020; Direktorat Jenderal Perundingan Perdagangan Internasional, 2018.

The table shows that IA-CEPA imposes a higher rate of tariff post elimination compared to IK-CEPA in trade sector. The positive effect of the policy is evident from the drastic increase of 28.62% (YoY) in Indonesian goods exports to Australia in 2021. However, it should be noted that even before the enactment of IK-CEPA, Indonesian exports to South Korea in the same year amounted to 37.8% (YoY), thus indicating favorable opportunities brought by IK-CEPA for increasing trade values for Indonesia in the future. Therefore, by obtaining a certificate of

origin approved by IK-CEPA, economic actors can benefit from applying preferential tariffs to reduce production costs, thereby improving industrial competitiveness and making Indonesian products more competitive through preferential treatment. This could positively affect the expansion of market access and access to goods and services in South Korea.

The third opportunities fostered by the IK-CEPA were raising the trade balance value with South Korea to become a surplus. Indonesia’s regulation to eliminate tariff barrier is another

opportunity to overcome the trade deficit with South Korea as the post-enactment trade value increased. Currently, Indonesia has a trade balance deficit with South Korea. According to Muhammad Takdir, the Head of the Center for Policy Strategy for the Asia Pacific and Africa Region of the Ministry of Foreign Affairs, South Korea implementation of more NTMs became one of the obstacles to Indonesian exports (Septyaningsih, 2022).

#### **Indonesia's Challenges in the IK-CEPA: A Comparison with the IA-CEPA**

Cooperation is not as simple as incorporating each other's practices in order to gain mutual benefits. Cooperation can be costly and not as profitable as the accumulation used (Andruseac & Hertug, 2015). For the same reason, countries construct cooperation based on legal agreements that have been settled by each respective party and manifested through fiscal policies. Assuredly, there remain some challenges in implementing cooperation agreements. The IK-CEPA is no exception in carrying both opportunities and challenges.

The first challenge of IK-CEPA pertains to the failure to achieve a trade

balance surplus. After IK-CEPA enactment, Indonesia's import value from the country grew 102.83% (YoY) to US\$ 9.42 billion in 2021 (Rahman, 2022) which at the same time illustrated a US\$6.2 billion deficit in trade goods with Australia. In other words, a significant increase in goods trade between Indonesia and South Korea in 2021 was a prolonged loss for Australia. In 2022, Australia was one of three countries (along with Thailand and China) with enormous trade balance deficits throughout the year up to US\$6 billion and the import value from Australia to Indonesia was higher than Indonesia's export value to Australia, namely US\$9.23 billion vs. US\$3.22 billion (Annur, 2023). Through this circumstance, cutting tariffs produces two simultaneous results: opportunities to increase export value and challenges to Indonesia's trade balance deficit, which will likely be detrimental if consumption dependence occurs.

Therefore, Indonesia currently experiences a trade deficit balance with South Korea. Table 2 below illustrates Indonesia's trade balance with South Korea from 2019 to 2021.

**Table 2.**

Indonesia's Trade Balance with South Korea from 2019 to 2021  
(million US\$)

Years	Values
2019	-1.186,90
2020	-341,80
2021	-446,70

**Source:** Indonesian Central Bureau of Statistics, 2022.

Indonesia marked the most significant deficit in trade balance with South Korea in 2019, amounting to -1,186.90 million US\$, which was the lowest in the past 32 years (Kusnandar, 2022). The deficit occurred due to the COVID-19 pandemic and persisted in the following years. Referring to Kang, Min, and Park (2021), the pandemic reduced Korea's GDP growth rate by more than 3 percentage points and resulted in the loss of approximately 460,000 jobs. It most significantly impacted private consumption, producing over 7 percentage point dip in growth rates. The pandemic forced South Korea to significantly reduce production activities that used raw materials exported from Indonesia, such as coal, steel plate products, clothing, plywood, and natural rubber. In addition, South Korea suffered from the weakest inflation in 2019 (0.4%) since 1966 (Nugroho, 2019). Inflation was induced by trade war uncertainty and a downturn in the global technology cycle, which dampened consumer demand.

Trade activity is more dynamic than investment due to the presence of external factors that substantially impact trade values. There remains possibility, albeit smaller than Indonesia-Australia context, for Indonesia to fail in overcoming trade balance deficit with South Korea if IK-CEPA is not optimally implemented or if uncontrollable external variables (e.g., economic inflation impacting lower private consumption) exist in both countries. Therefore, it is likely that IK-CEPA will exacerbate trade deficit between Indonesia and South Korea

Secondly, apart from the economic value, Indonesia may face the challenge of maximizing the use of IK-CEPA for

Micro, Small and Medium Enterprises (MSMEs). As mentioned earlier, the IK-CEPA also applies to implementing economic cooperation, including support for developing MSMEs. The tariff elimination is certainly of positive value for MSMEs in opening their product markets to South Korea. Trade cooperation agreements, such as the IK-CEPA and IA-CEPA also create opportunities for MSMEs to market internationally. The Ministry of Commerce of the Republic of Indonesia has FTA Centers in five commercial cities—Jakarta, Bandung, Surabaya, Medan, and Makassar—to increase the use of international trade cooperation programs, encourage entrepreneurial exports, and establish new exporters.

Nevertheless, MSMEs' harnessing IK-CEPA is far from straightforward. Indeed, MSMEs still face many challenges in capitalizing upon its opportunities. The Coordinator Deputy General Chairperson III for Maritime, Investment and Overseas Affairs Shinta W. Kamdan stated that many business actors, especially MSMEs, wish to use the IA-CEPA to export their products to Australia, but have not been successful due to such constraints as standard compliance (Mediatama, 2021). MSMEs still need to understand the standardization of national regulations, labels, content, and language to marketing their products internationally. Also, in the Re-Orient Webinar Series: IK CEPA Indonesian Diplomacy in the Middle of the Pandemic, the Ambassador of the Republic of Indonesia in Seoul, Umar Hadi stated that there are three main complaints from South Korean businessmen against Indonesian exporters. These are inconsistent product quality, subpar product

packaging with South Korean standards, and unmet Sanitary and Phytosanitary (SPS) standards. Therefore, another challenge for Indonesia is to equally engage potential MSMEs and provide them with essential guidance to gain opportunities with IK-CEPA.

## CONCLUSION

The IK-CEPA offers profitable opportunities for Indonesia's economic and trade development. The value of South Korean projects and foreign investments in Indonesia is much higher and more stable than those of Australia. This paper has demonstrated that while the value of goods trade between Indonesia and two countries (Australia and South Korea) increased, South Korea outdid Australia. In terms of trade balance, Indonesia experienced a trade deficit with both countries, but relatively comparable with South Korea.

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Accordingly, IK-CEPA has bestowed Indonesia with excellent opportunities to raise FDI value, trade values, and trade balance with South Korea to gain a surplus. It is important to note that the opportunity for a surplus trade balance can turn into a challenge if Indonesia fails to optimally harness the IK-CEPA and fails to prevent the trade balance from deficit or worse conditions. Indeed, this stems from the more dynamic trade activity than investment between Indonesia and South Korea due to the external factors that significantly impact trade values between two countries. The maximization and utilization of the best possible opportunities are required in the implementation of the IK-CEPA. In particular, it is absolutely vital to learn from the shortcomings of the IA-CEPA where MSMEs still face many challenges in harnessing the opportunities due to such obstacles like standard compliance.

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