Indonesia-China Trade Performance in the RCEP Forum

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Abstract: This study aims to map out Indonesia's export performance, the competitiveness of its commodities, and the position of some of Indonesia's flagship commodities in China. The research method used in this study is the Revealed Comparative Advantage (RCA) and the Constant Market Share Analysis (CMSA). The data is from the Indonesia Central Statistics Agency (BPS) and UN Comtrade for 4-digit HS products. The finding from this study indicates that Indonesia's trade balance with China for the last three years (2018-2020) has widened the deficit. Intense negotiations with China are necessary to open up trade access to overcome the trade deficit. The Government is encouraged to launch the development of flagship products with high market values, such as chemicals, machinery, electricity, and textiles. In addition, the national downstream program for mineral and metal products is encouraged to do more robust plans, including considering attracting new industrial investment from China.

Keywords: Competitiveness, Featured Products, Strategy.

1. Introduction

In order to respond to several dynamics of changes in the world economy and strengthen an open global market as a fundamental part of the global economic recovery, the Government of Indonesia signed the Regional Comprehensive Economic Partnership (RCEP) on November 15, 2020. The RCEP agreement was initiated by Indonesia when it became the Chair of ASEAN in 2011, and Indonesia was then assigned to be the Chair of the RCEP negotiation. The RCEP is trade cooperation carried out by several ASEAN countries and ASEAN trading partners. The RCEP is a free trade commitment among its members. The main principle of this partnership and the construction of free trade cooperation is to create as many benefits as possible by optimizing the networks of countries involved (ADB, 2022). One of many bilateral cooperations available in the RCEP is the bilateral trade between Indonesia and China. The implementation of the RCEP Agreement, which is targeted to be fully ratified in the first quarter of 2022, is becoming more critical amid global economic shocks caused by the US-China trade war, the pandemic of Covid-19, and the Ukrainian War. To face the upcoming implementation of this agreement, it is crucial for Indonesia to prepare some strategic steps in anticipative efforts when it is implemented and to maximize the opportunity provided by the RCEP Agreement. Some studies conducted by several agencies recently recommended that participating in the RCEP agreement will bring positive impacts to Indonesia.

One of them is connecting Indonesia to the global value chain network of other RCEP members, such as China, Japan, South Korea, Australia, and New Zealand, as well as other ASEAN member countries. However, the problem faced by Indonesia is the existence of export goods that have high competitiveness but are difficult to enter the market of RCEP member countries. In addition, there are potential export goods that have low competitiveness and are still difficult to enter the markets of RCEP member countries. From the distribution of Indonesia’s exports to countries that are members of the RCEP forum, most of Indonesia’s exports are still going to China, Japan, South Korea, and India. Therefore, this is a challenge for the Government of Indonesia, how Indonesia can open some access and market its export products to these countries, especially China. China is important for Indonesia since its high demand for natural resources and manufactured products. Likewise, the Government needs to make some breakthroughs to reduce product importation from China. Therefore, conducting a study to map out Indonesia's good exportation to China is necessary. As a country with high economic growth, China has become the largest country among the RCEP members that absorbs
many Indonesian products. Indonesia's exports to China in 2020 are more than USD14 billion. The following is an illustration of the proportion of Indonesia's exports to several RCEP member export destinations including India (Ferrantino, Maliszewska and Taran, 2019).

**Figure 1: Proportion of Indonesian Exported Goods to Export Destination Countries**

Source: World Bank, 2020.

Considering the value of Indonesia's exports and imports, optimizing trade cooperation with RCEP member countries is very strategic, especially with China. Indonesia's export growth, especially non-oil and gas, continued to experience an upward trend, even though the trade balance was in deficit. Specifically, Indonesia's exports to China experienced a relatively large trade balance deficit. In the future, it will become an opportunity and a challenge for the Indonesian Government to increase its exports to China by increasing its competitive products and how to downstream its several natural products. Through this study, we hope that Indonesia can determine the position of its leading commodities and formulate its trade policies with China.

**Research Purposes:** This study aims to map Indonesia's leading commodities' export performance and competitiveness with China. This research is also expected to describe the indicators and positions of many Indonesian commodities (HS 4 digits) against China. We hope the indicators can contribute to preparing some strategies for Indonesian delegates who do some trade negotiation activities with China.

**Research Output:** By reading this paper, we hope readers can:
- Identify or map out Indonesia's export performances and the competitiveness of its commodities with China (HS 4 digits).
- Position every Indonesia's commodity with China and some strategies that Indonesia can take.
- Recommend policies related to Indonesia's export performances and its competitiveness with China.

The three outputs above are beneficial for the line ministries and the Indonesian embassies and Trade Attaché in China to do some diplomatic ties in upscaling Indonesian exports.

2. **Research Method**

This research uses exploratory research and descriptive methods. This method uses the *Revealed Comparative Advantage* (RCA) and *Constant Market Share Analysis* (CMSA) approaches. The RCA approach
analyzes the comparative competitiveness of all Indonesian export commodities to China. The RCA formulation can be found as follows: (Tambunan and Wijanarko, 2000)

\[
RCA = \frac{\left(\frac{X_{ia}}{\text{total } X_{ia}}\right)}{\left(\frac{X_{iw}}{\text{total } X_{iw}}\right)}
\]

Where:
\(X = \) export or export value
\(i = \) type of commodity
\(a = \) country of origin
\(w = \) world

If the RCA < 1 or close to 0, it means that the competitiveness of the commodity is weak, and if the RCA > 1, then the competitiveness is strong. The higher the RCA of a commodity, the stronger its competitiveness. Calculating the CMSA or the constant market share model is used to determine the competitive advantage or competitiveness of exports in the world market from a producing country to some competing countries. This model shows a calculation that looks at competitiveness and the main products of these products against changes in world demand or trading partner countries (Balassa, 1989). The CMSA formulation is as follows:

\[
\text{CMSA} = \left[ \sum_{jk} \Delta \left( \frac{X_{ijk}}{X_{jik}} \right) \cdot \frac{X_{ijk}^0}{X_{jik}^0} \right] + \left[ \sum_{jk} \Delta \left( \frac{X_{ijk}}{X_{jik}} \right) \cdot \frac{X_{ijk}^0}{X_{jik}^0} \right] + \left[ \sum_{jk} \Delta \left( \frac{X_{ijk}}{X_{jik}} \right) \cdot \frac{X_{ijk}^0}{X_{jik}^0} \right]
\]

The CMSA Calculation Consists of 3 Criteria: The Competitiveness Effect (CE): a gain or loss in market share that shows the competitiveness of a product. The calculation measures the change in the share of the exporting country in the import destination market (IA) multiplied by the \(j\) share of imports from trading partner countries or export destination countries in the world market (IB). Or, the CE can be obtained by calculating the change in exporting countries divided by destination market imports (IA) multiplied by the initial share of imports of partner countries in world trade (IB).

\[
\sum_{jk} \Delta \left( \frac{X_{ijk}}{X_{jik}} \right) \cdot \frac{X_{ijk}^0}{X_{jik}^0} = \Delta \left( \frac{X_{ijk}}{X_{jik}} \right) \cdot \frac{X_{ijk}^0}{X_{jik}^0}
\]

\(X_{ijk} : \) export for commodity \(j\) from country-of-origin \(k\) (e.g. Indonesia) to destination country \(i\)
\(i : \) export to destination country
\(j : \) type of commodity
\(k : \) country of origin

A positive CE means that the product's competitiveness is higher in the export destination country. While a negative CE indicates that the product's competitiveness is weaker in the export destination country. A zero CE means that the product does not have the competitiveness of the product in the export destination country.

Initial Specialization (IS), is an indicator that shows that certain products have characteristics in a particular market that can be developed.

\[
\sum_{jk} \Delta \left( \frac{X_{ijk}}{X_{jik}} \right) \cdot \frac{X_{ijk}^0}{X_{jik}^0} = \Delta \left( \frac{X_{ijk}}{X_{jik}} \right) \cdot \frac{X_{ijk}^0}{X_{jik}^0}
\]

\(X : \) world’s export
\(X_{ijk}^0 : \) exports of commodity \(j\) of competing countries from country-of-origin \(k\) (e.g. Indonesia) to destination country \(i\) in the initial period (0).

The Initial Specialization (IS) is calculated from the change in imports of world trading partner countries (IIA) multiplied by the share of the country of origin in the import of the destination market (IIB). If the IS result is positive, it has more power to enter the market in the destination country. If the IS is negative, it has less power to enter the market in the export destination country, and if the IS result is zero, it does not have the power to enter the market in the export destination country. Adaptation (A) is an indicator that shows the ability of the product (supply of export) to respond or adjust due to changes in world demand.
The Adaptation (A) is obtained by calculating variations across changes in exporting country’s market share (IIIB) and changes in the market share of trading partner countries for certain specific products in world imports (IIIA). If the A is positive, it indicates that the products are more able to adapt to market tastes in the export destination country. And if the A is negative, it shows that the products are unable to adapt to market tastes in the export destination country. A zero means that these products cannot adapt to market tastes in the export destination country.

The outcome criteria of RCA and CMSA can be described as follows:
- If RCA > 1 and CMSA > 0, it means Great or good
- If RCA > 1 and CMSA < 0, means Sunset or
- If RCA < 1 and CMSA > 0, means Sunrise
- If RCA < 1 and CMSA < 0, means Suffer

From the results of the calculation of the RCA and the CMSA for each country, when displayed between Indonesia and China’s partner country, it will be displayed as shown in the following table:

**Table 1: RCA and CMSA Criteria**

| Indonesia | Suffer | Sunset | Sunrise | Great |
|-----------|--------|--------|---------|-------|
| Suffer    | Trade  | FDI Inflows | FDI Inflows | FDI Inflows |
| Sunset    | FDI Outflows | Trade | FDI Inflows | FDI Inflows |
| Sunrise   | FDI Outflows | Share | Trade | FDI Inflows |
| Great     | FDI Outflows | FDI Outflows | FDI Outflows | Trade |

**Source:** (Verico, 2020).

An ideal position of trade relations (export or import) between Indonesia and its partner countries is if the calculation of the RCA and CMSA of Indonesian products, or industries, shows a value equivalent to the value of the products or the value of industries of partner countries. However, if the values obtained differ, investment relations are the best form of bilateral relations. Indonesia can invest in partner countries if Indonesia's products are better than partner countries' products and vice versa. This study used 4-digit HS goods export data with the frequency of data used from 2016 to 2020. We obtain data from several sources, including UN Comtrade, the Indonesia Central Statistics Agency (BPS), and other sources. To deepen the analysis, we added some additional information to this study, such as references, literature, electronic media, and reports.

3. Literature Study

A total of fifteen countries of ASEAN countries, plus Japan, Australia, New Zealand, South Korea, and China, signed the Regional Comprehensive Economic Partnership (RCEP) agreement on November 15, 2020. The RCEP has become the largest multilateral trade forum in the world, initiated by Indonesia while it was the chairman of ASEAN in 2011. The RCEP was launched based on the spirit of strengthening trade and investment among the RCEP’s members. This commitment is also expected to contribute more to minimizing regional economic inequality in the region (Clarissa and Gandara, 2020). More specifically, Indonesia expects its bilateral ties with China to improve its trade balance and broaden access to the transaction of goods between the two countries. Indonesia’s trade policies have changed over the decades. Indonesia had withdrawn from global trade activities in the early 1960s. However, it re-opened in the next decade. Indonesia’s trade policy development is increasingly open to the global economy with various liberalization policies.

This phase began in the early 1980s as the first step of its transformation for Indonesia to open its trade policy. These liberalization steps were taken in the form of international trade cooperation such as bilateral, regional, and global cooperation (Tsurayya, 2013). The trade liberalization came through free trade agreements (FTAs). With this free trade, Indonesia is expected to increase its GDP and investment to achieve
household welfare. Bilateral and regional cooperation such as ASEAN, the RCEP, and others were expected to create more trade activities. However, Indonesia had a smaller advantage over its trade liberation than other ASEAN countries. A simulation of full liberalization in the ASEAN positively impacts Indonesia's trade volume, exports, and imports. However, the percentage increase in imports was higher than the increase in exports, so it negatively impacted Indonesia's trade balance (Syadullah and Ardiansyah, 2014). On the other hand, the survey results (Kawai and Wignaraja, 2013) of several companies in mainland China and Japan.

The Republic of Korea, Malaysia, the Philippines, Singapore, and Thailand show higher estimates of the use of the FTAs by companies. It shows that around 32 percent of companies have taken advantage of the FTAs and have made better plans. The survey also revealed that the FTAs require a constant ongoing cost. Large companies can collect financial and human resources better than small and medium enterprises (SMEs). Another advantage of trade cooperation, based on some studies, is that trade cooperation will bring several benefits to Indonesia. Based on the Indonesia Trade Assessment and Development Agency (BP3) analysis of the Ministry of Trade, trade cooperation can bring welfare improvement, but at the same time, there will be an increase in the trade balance deficit with partner countries (Romarina, 2016). Further, studies suggest that Indonesia should strengthen its capacity to utilize the regional value chain considering that there are 6,050.

Indonesian custom tariffs (traded goods) are related to strong export and import connections to many trade areas. In 2019, the Indonesian Finance Ministry studied the impact of trade cooperation (the RCEP) on the Indonesian economy. This study uses the Computable General Equilibrium (CGE) model. The result of this study indicates that the RCEP will increase Indonesia's Gross Domestic Product (GDP) by only 0.05 percent between 2021 - 2032, much smaller than the benefits obtained by other RCEP countries. Vietnam gets 0.66 percent, South Korea 0.51 percent, Malaysia 0.35 percent, and Thailand 0.21 percent. However, further studies show that if Indonesia decides to leave the RCEP, its economic growth (GDP) will fall by -0.07 percent. Therefore, Indonesia has no choice but to remain a member of the RCEP and continue making structural adjustments to improve efficiency and competitiveness. Ulfah's (Ulfah and Felianty, 2017) research shows that the competitiveness of Indonesian products is weak compared to most other RCEP member countries. Therefore, the Indonesian Government must improve its product competitiveness and, at the same time, optimize its membership in the RCEP. The simulation shown in this study indicates that implementing the RCEP agreement is expected to improve trade performance, GDP, and welfare of most member countries, including Indonesia.

According to Moenardy (Moenardy et al., 2020), several strategies need to be carried out by the Indonesian Government in terms of regional trade cooperation. There are two strategies, either internal or external. Internal strategies include, among others, the Government must optimize cooperation and services to exporters. One of them is conducting labor training to improve quality products, creating and producing superior products that can dominate the market, and protecting farmers regarding seeds monopoly and medicines for plants. The external strategy includes, among others, the Government should negotiate with partner countries, such as China, so that there is no outpouring of China's products to Indonesia. Likewise, it is necessary to make regulations with multinational companies to empower Indonesian workers if they are to build industry in Indonesia (Kemendag, 2015). Current global economic development brings many impacts on Indonesia's economic growth. Therefore, it is necessary to map out Indonesia's competitiveness and trade specialization with Indonesia's main trading partners to determine the pattern of trade between countries (Romarina, 2016). Romarina's study explores Indonesia's comparative advantages with its major trading partners to identify Indonesia's leading sectors that contribute to its economic growth. Apart from identifying the leading sectors, Romarina also identifies the weaker sectors (looser sectors).

In his study, Romarina analyzes the trading model consisting of the gravity model, the Ricardian model, the Heckscher-Ohlin model, the Standard Trade model, and the New Trade model. These models analyze Indonesia's bilateral patterns with its main trading partners. In his study, Romarina concluded that Indonesia's trade pattern with its main trading partners, China, Australia, and the US, follows the Heckscher Ohlin (HO) model. The evidence shows each country's sectoral composition of export and import data exports abundant and intensively produced products. However, by looking at the size of the economy and the distance between countries, it is known that Indonesia-China trade relations follow the gravity model. Moreover, the higher share of exports and imports in the crude oil industry between Indonesia and Australia

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indicates that the trade pattern follows a new trading industry that signals intra-industry trade (Hasanah, 2020). In another reference, Galura (Cakra and Munandar, 2020) showed a sample of how brewed tea could be the world’s most consumed beverage after water. The tea commodity has four types: Bulk Green Tea, Packed Green Tea, Bulk Black Tea, and Packed Black Tea. Even though Bulk Black Tea has the lowest average price, it has the highest demand and high growth of import value per year. Moreover, Russia is the leading Indonesian destination country for this commodity.

Using multiple linear regression, Galura aims to analyze the competitive position of Indonesian bulk black tea in the global market by applying the CMSA method. Trying to find factors that affect its competitiveness in the Russian market. The analysis used in this study uses the Global Trade Analysis Project (GTAP) application which predicts the impact of 17 countries with 43 products. The analysis using the CMSA method shows that Indonesia's competitiveness is low among some major exporting countries and has a negative trend. Then, based on multiple linear regression analysis, it shows that price is the most influential factor in the competitiveness of Indonesian bulk black tea in the Russian market. It means that the higher the price, the lower the competitiveness of Indonesia for bulk black tea commodities. In another study, Suwarno (Suwarno et al., 2012) used the CMSA to analyze the source of growth of tuna exports in international markets. Based on his study, Suwarno found an increase in the export of Indonesian tuna commodities in the international market due to the soaring of the international export market. The competitiveness of some Indonesian commodities also increased, such as frozen tuna, yellowfin tuna, skipjack tuna, tuna ness, and preserved tuna. Suwarno concluded that a critical factor that affects the quantity of tuna exported is the Gross National Product and the amount of tuna production in Indonesia.

4. Results and Discussion

Indonesia-China bilateral relations rapidly increased in the last 20 years. Total trade between Indonesia and China increased 18 times, from US$4 billion (2001) to US$73 billion (2020). However, if we look at the growth of Indonesia's exports to China, it experienced some fluctuation and had a downward trend. Since 2008 Indonesia's trade balance with China has a growing deficit. Since 2008, Indonesia's imports of products from China have increased more than Indonesia's exports. The Indonesian trade deficit also occurred with other countries such as South Korea, Australia, New Zealand, Singapore, Thailand, & Laos.

Figure 2: Indonesia-China Trade Balance, 2001-2020

Source: Trade Map, 2021 (Ragimun et al., no date)

The fluctuations of some of Indonesia's export to China are in line with movements in world commodity prices, especially raw commodities. Most of Indonesia's exports to China are unprocessed natural commodities, such as oil, gas, coal, iron ore, and CPO (palm oil). Some commodities prices decreased in early 2018, such as oil, gas, coal, and CPO, except iron ore which had an upward trend. It impacted the total value of Indonesia's exports to China. If we look at Indonesia's competitiveness with China, of the 1259 export products (HS Code 4 digits) to China, there are 454 flagship products (36%) and 805 non-flagship products (64%). Only ten products from the 454 flagship products bring significant changes in export values. Ten flagship products of Indonesia in 2019 which have an upward trend and have ‘Great’ criteria (see attachment)
are iron ore (ferro-alloys), oil and gas, nickel, palm oil (CPO), coal, lignite, pulp, stainless, aluminium, and others. These flagship products, when we put them on the map, will look as follows;

**Figure 3: Competitiveness of Indonesia's Commodities to China in 2020**

![Figure 3: Competitiveness of Indonesia's Commodities to China in 2020](image)

**Source:** Trade Map, 2021 (Ragimun et al., no date)

If we want to make a short analysis on coal, for example, coal (HS Code 2701) has a high export value. However, it is no more flagship and becoming a sunset product since the world's attention to climate change and clean energy. Meanwhile, products with HS Code 2701-2702 Lignite, even though their export values are not as significant as coal's, are becoming flagship products since they are in the "great" category. If we move to Ferro-alloys with high CMSA and RCA scores, whereas the RCA score is higher than 1, we could claim that it is a flagship product. However, if we see coal and palm oil commodity, we can see that both have low CMSA score even though their RCAs is higher than 1. From this perspective, we can say that even though these two products are flagship commodities, their charm has begun to wane over time. Moreover, here, we conclude that Government is supposed to implement different policies and treatments for each commodity depending on their score on the map.

Sixty-eight flagship products from Indonesia to China (HS 4 digits) have the "Great" criteria. It means that these products still have the opportunity to scale up in quantity, market value, and market share. The majority of them are natural raw commodities, such as oil, gas, coal, lignite, nickel, fishery products, CPO, and others. Besides, several manufactured commodities such as textiles and garments, footwear, food and beverages, and household appliances still have the opportunity to enter the market by raising their quantities and market values. In addition to Indonesia's flagship commodities which have the "Great" category, some non-flagship commodities also have the "Sunset" category. There are 19 "Sunset" commodities, meaning they have a downward trend in terms of quantity, value, and market share in China. These products include coal, textiles, paper, raw rubber, copper wire, plywood, and several others. Since being categorized as "Sunset" commodities in 2014, the category did not change until 2019. These product categories are not flagship products. To increase their market share and make them have "sunrise" or "great" categories, the role of the Government is very necessary. Especially to encourage the downstream program of this raw material exportation into derivative products. By doing this program, Indonesia's commodities will get higher values in the market. Negotiating and opening access to these commodities in China or other RCEP members are important. The following are some products that still have the opportunity to increase the market values and quantities in China.
Table 2: Value and Number of Exported Products to China that Need to be Improved

| NO | HS Code | Products | China Values (USD Millions) |
|----|---------|----------|----------------------------|
| 1  | 01-05: Animal Products | 13 | 70.08 |
| 2  | 06-15: Agricultural Products | 34 | 3,378.36 |
| 3  | 16-24: Processed foods | 17 | 316.05 |
| 4  | 25-27: Mineral Products | 24 | 10,559.67 |
| 5  | 28-38: Chemical Industries | 60 | 1,939.93 |
| 6  | 39-40: Plastics/rubber | 19 | 402.69 |
| 7  | 41-43: Leather, fur and its products | 6 | 23.35 |
| 8  | 44-49: Wood products | 28 | 2,789.87 |
| 9  | 50-63: Textiles | 42 | 267.39 |
| 10 | 64-68: Footwear dan headgear products | 13 | 529.55 |
| 11 | 69-71: Stone and shard products | 18 | 20.39 |
| 12 | 72-83: Metal products | 65 | 3,570.50 |
| 13 | 84-85: Electrical machines and tools | 67 | 358.34 |
| 14 | 86-89: Transportation products | 12 | 65.22 |
| 15 | 90-99: Other products | 36 | 180.14 |
| Total | 454 | 25,105.61 |

Source: UNComtrade, 2020.

All 454 commodities that can be upscaled to become flagship commodities have a large value, which is USD 25,105.61 million. The attention and effort of the Government are essential to increasing Indonesia’s market share. Currently, China is the country that absorbs a lot of Indonesia’s flagship commodities. The existence of bilateral relations between Indonesia and China and Indonesian membership in the RCEP makes it Indonesia easy to negotiate commodities that can enter the Chinese market. The commodities are agricultural, mineral, chemical, wood, textile and garment, steel products, machinery, and electrical equipment.

5. Conclusion and Recommendations

Conclusion: The total value of Indonesia's trade with China for two decades (2001-2020) experienced a rapid growth rate of 18 times. However, this growth rate was not followed by an improvement in the Indonesia-China trade balance because from 2008 to 2020, Indonesia's trade balance with China experienced a relatively sharp deficit. The analysis results show that several Indonesian flagship commodities have the potential to raise Indonesian trade values. From 1259 export commodities, Indonesia has 454 flagship commodities with 4-digit HS (36%). Indonesia's flagship commodities include oil, gas, coal, lignite, nickel and CPO. These commodities are excellent in the “Great” category. At the same time, Indonesia also has some commodities that are not-flagship commodities but have large trade values, such as garments, paper, coal briquettes, copper, and rubber. They are commodities in the "Sunset" category.

Recommendations: Indonesia needs to intensify communications with China and several RCEP members to overcome its trade balance deficit. We suggest Indonesia start with countries with strong trade relations that significantly impact Indonesia’s trade performance, such as China, South Korea, Australia, and New Zealand. Indonesia also needs to scale up its opportunities with other ASEAN members, especially Thailand, Singapore, and Laos. Focusing on China under the RCEP cooperation, Indonesia needs to raise its trade values, especially for some of Indonesia's flagship commodities such as CPO, oil, gas, coal, and lignite. Lastly, strengthening competitiveness and renegotiating some of Indonesia's non-flagship commodities are two things that cannot be put off any longer, especially for goods that experienced a decline in demand in China, such as textiles and paper.
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