

# CHAPTER I

## INTRODUCTION

### **A. Background of Research**

Indonesian economy has reached the stage of maturity. It is characterized by the increasing the number of investments annually. In addition, Indonesia has an opportunity to develop its economy in the future. One of such opportunities comes from the implementation of AEC (ASEAN Economic Community) in 2015. The AEC is expected to turn ASEAN region into a single market and production base. ASEAN Economic Community is expected to make ASEAN become a more dynamic and competitive region with new measurements and mechanisms to strengthen the implementation of economic initiatives which have already existed. An ASEAN single market and production base shall comprise of five core elements, namely: (i) free flow of goods; (ii) free flow of services; (iii) free flow of investment, (iv) free flow of capital, and (v) free flow of skilled labor.

Indonesia ranks five out of 8 of ASEAN countries in terms of industrial competitiveness. The Indonesia's competitiveness comes after Singapore, Malaysia, Thailand, and Vietnam and before Cambodia, Philippines and Brunei.

Here is a table of world competitiveness rank which consists of some countries taken randomly.

**Table 1.1**  
Word Competitiveness Rank of 14 Countries

Name of Country	2003	2004	2005	2006	2007
<b>United States</b>	1	1	1	1	1
<b>Singapore</b>	4	2	3	3	2
<b>Hongkong</b>	10	6	2	2	3
<b>Switzerland</b>	9	14	8	8	6
<b>Australia</b>	7	4	9	6	12
<b>China</b>	27	22	29	18	15
<b>Taiwan</b>	17	12	11	17	18
<b>Malaysia</b>	21	16	26	22	23
<b>India</b>	42	30	33	27	27
<b>South Korea</b>	32	31	27	32	29
<b>Thailand</b>	28	26	25	29	33
<b>Philippines</b>	41	43	40	42	45
<b>Indonesia</b>	49	49	50	52	54
<b>Venezuela</b>	51	51	51	53	55

Sources: International Institute for Management Development,  
World Competitiveness Yearbook, 2008 *Lanskap Ekonomi Indonesia* book, p. 36.

**Table 1.2**  
Weighted Ranking of ASEAN Competitiveness 2008-2015

Country	Year						
	2008-2009	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	2014-2015
<b>Brunei</b>	39	32	28	28	28	26	26
<b>Cambodia</b>	109	110	109	97	85	88	88
<b>Indonesia</b>	55	54	44	46	40	38	38
<b>Malaysia</b>	21	24	26	21	25	24	24
<b>Philippines</b>	71	87	85	75	65	59	59
<b>Singapore</b>	5	3	3	2	2	2	2
<b>Thailand</b>	34	36	38	39	38	37	37
<b>Vietnam</b>	70	75	59	65	75	70	70
<b>Average</b>	50.5	52.625	49	46.625	44.75	43	43

Sources: The Global Competitiveness Index Report. (www.weforum.org)

Table 1.1 shows the critical condition of Indonesian economic competitiveness in global area. Indonesia's competitiveness rank continuously moved downward and decreased from 2003 until 2007.

Table 1.2 illustrates the competitiveness of ASEAN countries from 2008 until 2015 in which the competitiveness index of Indonesia shows changes from 2008 to 2015. The most substantial movement occurred in 2011; in 2011 the competitiveness rank of Indonesia raised 10 digits, from 54 to 44. This happened because of the efforts made by the government and all society in order to compete in the global market.

Indonesia is a country in which the economy is mostly supported by SMEs (Small and Medium Enterprises). The number of SMEs in Indonesia has reached about 56.5 million in which 99.8 percent of them are MSMEs (Micro, Small and Medium Enterprises). The need to increase the industrial sector's competitiveness of either small or large businesses is necessary because those sectors can boost the nation's economy and welfare. And generally, MSMEs can create opportunities for people who need jobs in times when it is difficult to find a job. In Act No. 20 of 2008 Article 3 about Micro, Small and Medium Enterprises:

*“Usaha Mikro, Kecil, dan Menengah bertujuan menumbuhkan dan mengembangkan usahanya dalam rangka membangun perekonomian nasional berdasarkan demokrasi ekonomi yang berkeadilan”. UU No20 tahun 2008 pasal 3.*

The existence of MSMEs is expected to support the national economy on the growth of government's revenue due to the contribution of the industrial and service sector through taxation.

The Special Region of Yogyakarta (D.I. Yogyakarta) is one of the provinces in Indonesia which is known as the city of tourism. It has plentiful natural potentials and adequate facilities which support the economy. D.I. Yogyakarta's geographical condition, which consists of mountainous, coastal and urban areas, offers bigger opportunities to expand the economy. D.I. Yogyakarta is also known as a city that is rich in cultural potentials. However, despite the opportunities mentioned earlier, there are also significant challenges for D.I. Yogyakarta in facing the AEC, especially for MSMEs, namely, how MSMEs in Yogyakarta can optimize the potential which they already have in order to compete or even prevail as the main actors in AEC, and what major roles are taken by MSMEs in DIY in optimizing the potential. Before improvements of the competitiveness can take place in order to compete in AEC, we should first know the position in the competitiveness index.

This paper focuses on the vital factors which influence MSMEs in DIY's competitiveness index in facing the AEC, these include internal and external factors. The examples of internal factors include the low level of public awareness in DIY which has become a hindrance to community's readiness in facing the AEC. The lack of human interest to compete will eliminate them from economic development. The lack of Information and awareness, and lack of

skilled human resources has become an obstacle to achieve the economic development. And the examples of external factors include the fluctuating price of energy source, the fluctuating interest rates, the lack of infrastructure, etc. These factors as hindrances have become the prerequisite to be fulfilled so as to increase D.I. Yogyakarta's economic development.

#### **B. Limitations of The Study**

In order to conduct a research which is consistent with the objectives, hence the writer sets the following restrictions:

1. The research is done only on micro, small and medium scale enterprises that are related with tourism sector in DIY.
2. The samples are taken from the micro, small and medium scale enterprises which perform production activity.

#### **C. Formulation of Problem**

In this research, the writer has some formulation of problems, namely:

1. What is the index of the competitiveness of MSMEs in D.I. Yogyakarta in facing the AEC?
2. What are the internal and external problems faced by MSME agents in D.I. Yogyakarta in facing the AEC?

#### **D. Purpose of Research**

This research aims at:

1. Knowing what the competitiveness index of MSMEs in D.I. Yogyakarta to compete in the event of AEC.

2. Understanding the internal and external problems faced by MSME agents in D.I. Yogyakarta on the facing of AEC.

#### **E. Advantage of Research**

The benefits of this research are as follows:

1. Increasing the interest to and the readiness of MSMEs in DIY to compete in AEC.
2. Optimizing the AEC event as a challenge to developing Indonesian economy in the global economic interactions.
3. As a reference for the stakeholders and the authorities to strengthen Indonesian economic competitiveness especially for MSMEs in DIY in dealing with the ASEAN economic community.