CHAPTER I

1.1. Introduction

1.1.2 Background

The invention of technology, especially the internet, has become a vital momentum and also, at the same time, acts as a turning point for all kinds of changes in this world. Whether we realize it or not, almost every aspect of our life has changed into a digital transformation. Starting from the social aspect, education aspects, including the economic aspect, have now been transformed into digital. The digital economy is overgrowing with the penetration of smartphones and the internet across different levels of society across the world. It has now completely changed the way people buy and sell goods. Many of today's economic and business activities are no longer fixated on conventional methods, but both have started to adopt technology into their various activities.

Based on the definition, the digital economy is a general term used to describe a market that focuses on digital technology supported by the internet and usually involves the trading of goods or services via e-commerce (OECD, 2017). Furthermore, in short, the real form of this digital economy is manifested in the form of electronic commerce (often called e-commerce), which includes all commercial activities carried out online through digital channels in the form of the internet. Besides giving a broader scope, e-commerce is considered more efficient than conventional methods because its presence is considered capable of providing more excellent economic benefits for its actors. Therefore, in recent years, many e-commerce companies and platforms have emerged, which were specifically established to accommodate these electronic-based trading activities.

When it comes to e-commerce companies and platforms that are booming, we cannot deny that one of the biggest players in this industry is Alibaba Group Holding Limited. Alibaba Group Holding Limited is the fastest growing e-commerce company from China made by Jack Ma in 1999. This company gives a significant impact on the development of e-commerce in the entire world. In the beginning, Alibaba is an e-commerce company that only focuses its business on the retail industry through services via a web portal. But not even 20 years since the company was founded, Alibaba has grown to such an extent. It is no exaggeration to say that it has dominated the entire e-commerce landscape in China.

Alibaba has grown into a giant company and has its superiority, enabling them to dominate the competition in the global e-commerce industry. Based to the US Securities and Exchange Commission (SEC), China's e-commerce site 'Alibaba' has become the world's largest retail platform. Not only that, but Alibaba also has outpaced Walmart that posted revenues of $482.1 billion for its fiscal year ending January 2016 (Kwak et al., 2019, p. 116). Transactions recorded on Alibaba's online platform have drawn a figure of 248 billion USD, which even exceeds the number of eBay and Amazon transactions combined (WSJ.com News Graphics, n.d.).

Based on this success, Alibaba is now no longer just a retail e-commerce company. They have also expanded their business into different business fields, such as online payment services, computing technology, and many others. Even Forbes stated that in terms of the number of companies handled, it is impossible to deny that Alibaba is the largest online commerce company in China and the world (Wright, 2015).

We can see how big the business Alibaba has in the e-commerce industry, especially in its home country, from many achievements. But no matter how big and successful a company is, they all have the same basic characteristics as a business entity. Every big company wants to expand its market share and seek greater profits. Alibaba also has the same justification.

After successfully conquering the e-commerce market at the local level, in recent years, Alibaba has set new corporate goals. Alibaba starts to expand its market coverage and domination to a global level beyond its original domain in China.

Moreover, to make Alibaba the leader of all e-commerce companies and beat fellow competitors in the e-commerce industry. Alibaba uses its superiority to drive them to start internalization by expanding their company to global business. In actualizing its goals, Alibaba began to observe the e-commerce market share in Asia Pacific Region.

The expansion strategy chosen by Alibaba Group to initiate entry into countries in the Asia-Pacific region is quite different from expansion in the previous region. Alibaba Group prefers to invest in several local companies, especially companies that can support its primary business model in the e-commerce field—but not launching its e-commerce platform. Moreover, to anticipate the economic crisis and the start of market saturation in China, Alibaba Group, is targeting to find new, more dynamic markets outside of China's domestic market. Therefore, Alibaba Group Holding Ltd is very ambitious to accelerate its unique income source by exploiting the e-commerce market opportunities in the Asia-Pacific region.

In Alibaba's efforts to expand into the global market, choosing the location of the market destination country and the level of e-commerce sector establishment in it is the most crucial step that should be considered carefully. Because selecting the target country's location is one of the keys to the success of their expansion process. Furthermore, Alibaba sees the industry and e-commerce sector in Asia are considered to have enormous opportunities. Seeing this region is a "home" for developing countries whose e-commerce potential has not fully explored and can still be developed significantly. For example, Singapore, Thailand, Malaysia, and especially India, which have made very rapid progress in recent years and have begun to show their strength both in Asia itself and at the global level.

However, what makes it interesting, even though Alibaba has many choices of potential countries, which are also quite "developed" countries in the Asian region, Alibaba shows its interest in the Indonesian e-commerce market—competing with India, Singapore and Thailand. The Indonesian e-commerce market is currently receiving a lot of attention from big e-commerce players in the world. These conditions and opportunities also attracted Alibaba's attention to enter and make Indonesia a destination for expanding their market. The Indonesian e-commerce market itself is often touted as one of the ones experiencing the most significant growth and can develop very rapidly in the future. Indonesia is a unique country in many ways as the biggest archipelago globally, the largest Muslim majority country, East Asia Pacific's most vibrant democracies. Indonesia is the fourth most populated country in this world after the US, China and India. It makes sense if Indonesia has a large market size and a large consumer base, affecting consumer demand. The political condition in Indonesia from 2014-2018 considered stabile. Large market size and political stability becomes the main attraction why Alibaba is eager to expand its investment in Indonesia's e-commerce market.

As a result, Alibaba chose Indonesia as a host country to expand its market. Evidence of Alibaba's interest and belief in Indonesia has been realized in the form of investments they have made in local Indonesian e-commerce players. In 2017, Alibaba invested in Indonesia by buying shares from Tokopedia for USD 1.1 billion or around IDR 14.7 trillion (Indra, 2017). Tokopedia itself is one of the largest local e-commerce platforms in Indonesia, which is very capable. Since its founding in 2009, Tokopedia has dominated most of Indonesia's e-commerce landscape. It is no exaggeration to say that Tokopedia is currently the pioneer of the e-commerce industry and sector in Indonesia. However, before Alibaba acquired Tokopedia's shares, to be precise, in April 2016, this giant company also made a similar investment in Southeast Asia-based e-commerce platform Lazada for 1 billion USD, which even made them the majority shareholder. Although not from Indonesia, the writer feels the need to include

Alibaba's acquisition of Lazada in this research discussion. In Indonesia, Lazada is one of the most dominant e-commerce platforms and is always competing to become the number one shopping destination in Indonesia - along with Tokopedia. Indeed, Lazada's e-commerce base is focused on six countries in Southeast Asia. Still, if you look at the contributions from each of the six countries, it can be said that Indonesia is the one that contributes the most prominent role in the success of the platform. This means that Indonesia's support also influences Alibaba's decision to participate in investing in Lazada.

It turns out that the two investments made by Alibaba on Tokopedia and Lazada are the largest investment amount that Alibaba has ever made. Where respectively ranks third and fourth of all the largest investments Alibaba has made in other companies (Tech in Asia, n.d.). So far, Alibaba has often only made large investments in fellow companies and local e-commerce platforms from China. Another big investment made to outsiders is e-commerce from India. But even then, the amount is much smaller when compared to the amount that Indonesia received.

Looking at the investment phenomenon that Alibaba has made in Indonesia, this study seeks to analyze what factors the Indonesian e-commerce market has that makes Alibaba interested in investing in such a large amount. Because basically, there must be more than one factor that underlies a company as big as Alibaba's decision to make Indonesia the location for their market expansion destination.

1.2 Research question

The research questions that arise from the above background are, ***Why did Alibaba decide to appoint Indonesia as the destination for expanding its e-commerce market?***

1.3 Theoretical frameworks

In order to be able to answer and analyze the research questions that have been mentioned in the previous section, this study uses several theories and concepts.

a. Economic liberalism

The main perspective of this research is based on the theory of economic liberalism. Economic liberalism is a branch of the Theory of Liberalism which was born from a British economist named Adam Smith in 1976. Economic liberalism is a set of doctrines and principles aimed at managing the economy and markets to achieve maximum efficiency, economic growth and individual welfare through cooperation to avoid conflicts between countries and create interdependence. Departing from the basic assumption of John Locke and Adam Smith, the relationship between countries is considered the same as the relationship between citizens in a country. That each country has the same economic interests as humans. And peace is not impossible because every constitutional state will think rationally, namely for the achievement of each of these interests, each country will obey itself to an international law that will regulate their lives in international relations.

In the 70s, institutions around the world have developed rapidly. Countries are increasingly dependent on each other and are increasingly sensitive to the actions of other countries. In this case, international politics is a process in which actors in international relations mutually solve problems that arise in international relations. Even today, actors are not only the state, the world is in a cross between countries, NGOs, elite groups, MNCs and even individuals. Those who are bound by interdependence are forced to cooperate extensively. So the higher the level of cooperation and integration, the more difficult it will be for countries to withdraw from the commitments they have made because their people will realize the various benefits obtained by cooperation.

Interdependence between actors in international relations is well written in Susan Strange’s book "The Retreat of the state" which is able to shift the understanding of balance of power through economic integration cooperation. The progressive integration of the world economy, trough international production, has shifted the balance of power away from states and toward world market. Integration between countries through an economic dependence will be able to get rid of the balance of power between countries because; First, economic integration is able to turn a weak country into a stronger one because it is able to cooperate with many countries. Second, the situations are also able to change the pattern of relations in which the market and non-state actors have sufficient power to match the state. Third, there is no situation where one country is absolutely capable of controlling all relations between countries without the influence of large economic forces. In the study of International Political Economy (IPE), Susan Strange's statement of "non-state actors being now more significant than states themselves". Susan Strange argues in her book "The Erosion of the State" that the state's power has been eroded for example: in the finance sector, states no longer have the power to control their own currencies, because in reality today the balance of international trade impacts currency exchange rates as supply and demand can lead to an appreciation or depreciation of currencies. A country with a high demand for its goods tends to export more than it imports, increasing demand for its currency.

In the reality of economic Interdependence between actors in international relations, the concept of free trade cannot is always used. The concept of free trade that promoted by economic liberalism, which is released from the market mechanism, individuals who play the main role in economic activity, and government intervention must be minimized. However, state has a role in creating peace through its intervention to make relations between countries occur and create interdependence. This can happen if the government intervenes to regulate the free market. The concept of free trade promoted by economic liberalism refers to trade conditions oriented towards openness, including free movement between commodities, capital flows and labour. Adam Smith describes a liberal framework of thought that provides rational individual actors, believes in progress, and assumes mutual benefits. This theory believes that the market economy is the primary source of progress, cooperation and prosperity. Furthermore, the law of comparative advantage was developed by David Ricardo. He argues that free trade is a commercial activity carried out freely from national restrictions that will bring benefits to all participants because free trade can increase efficiency and increase productivity (Jackson et al., 2019, p. 232). When the obstacles that limit economic activity are removed, a positive sum-game will be created. And also the key to achieving all parties' welfare, be it individuals, companies or countries.

Different from mercantilism, they believed that the main actor is a state. Economic liberals believe in the importance of non-state actors' role, especially in the era of globalization and technological advances today. Ideally, in an entirely free trade system, each country naturally devotes its capital and labour to the aspects most favourable to its individuals. In short, although global economic activity does have various positive impacts on the state, the main objective of this economic liberalism assumption is more aimed at the interests of individuals. In reality, today, companies-especially multinational companies can carry out their activities without having to involve the state directly. For example, the transfer of capital that crosses territorial borders is currently carried out by various multinational companies worldwide.

When carrying out business activities that cross the territorial boundaries of a country, multinational companies, in reality, will not be separated from the concept of foreign investment or what is commonly referred to as foreign direct investment (FDI). Foreign investment can be defined as capital provided by residents of one country to another country's residents (Griffin & Pustay, 2015, p. 8).

Based on the definition issued by the IMF Balance of Payments Manual: Fifth Edition (BPM5), FDI refers to Investments made to obtain interests in companies operating outside the investor economy. Furthermore, in the case of FDI, the investor aims to have an effective voice in the company's management (IMF,1993). Also, there are two types of FDI:

1. Foreign Direct Investment

This type of investment is carried out to actively control property, assets, or companies located in the host country. Companies involved in FDI and own or control the value-adding activities of a country or more are called multinational corporations (MNCs). In addition to owning and managing foreign assets, MNCs usually buy resources in various countries, create goods or services in multiple countries, and then sell them in multiple countries.

Direct investment can be in the form of; the establishment of a branch company in capital importing countries; the establishment of a company in which the company from the investing country owns the majority of shares; the establishment of a company in an importing country which is solely financed by the company located in the investing country; establish a corporation in an investing country to specifically operate in another country; or putting fixed assets (active) in another country by a national company from an investing country (Jhigan, 2014, p. 483).

2. Foreign portfolio investment

This investment is the purchase of foreign financial assets (stocks, bonds and certificates of deposit) for purposes other than control.

In the last few decades, FDI has experienced very substantial developments where there has been a shift in foreign economic activity, expanding its focus from export and import activities. Since then, the company has continued to show enthusiasm for investing abroad and expanding its scope into the global market. In the book Global Political Economy, Theodore H. Cohn believes that the development of FDI is a "major weaver of the world economy", which is supposed to increase efficiency and employment and encourage innovation, competition and economic growth (Cohn,2016).

b. Paradigm Ownership, Location and Internationalization (OLI)

To understand why multinational companies are competing to invest and position themselves abroad, this frame of mind is equipped with the OLI model or what is commonly called the eclectic paradigm proposed by John H. Dunning in 1979. OLI model stands for Ownership Advantage, Location Advantage, and Internationalization Advantage. These three things are the factors that become the reasons for a multinational company to invest abroad.

1. Ownership advantages

Ownership Advantage can be the first and foremost capital that a multinational company must-have when it wants to do FDI. These companies must have their advantages in terms of their own before they can expand into the global market. This Ownership Advantage is certain advantages owned by the company, which allows them to have the higher competitiveness than other companies. These advantages are used to transfer and enlarge themselves beyond their national borders. These advantages can be in the form of many things, whether it is their good company reputation, strong brand, large company scale, or certain uniqueness. Including the owner of the company itself because it turns out that the company's owner can have an influence on the success of the company's investment. According to Dunning, preponderance in terms of ownership is a value and competitiveness that significantly affects its ability to conduct FDI. Without both, it would be difficult for an overseas company to expand itself to a global level.

2. Internationalization

Internationalization Advantage is carried out by internationalizing the company. They are expanding the company into a broader market share, hoping that when they internationalize, the company will get other benefits such as reaching new customers, automatically increasing their company's profits. In the long term, it is hoped that the advantages of internationalization will help improve the previous companies' competitiveness and ownership.

3. Location Advantages

Location Advantage leads to the question of where the multinational company should invest its investment capital. Because as the finalization stage of FDI, this location selection is a critical factor for the company's internationalization process. The location chosen must have an advantage that makes it value-added compared to other locations, be it in economic opportunities, development opportunities for companies, or perhaps the uniqueness of a region. In essence, the company must choose a location that can bring and offer them an advantage. According to the eclectic paradigm by Dunning (1993), location advantages include benefits arising from the host country's factor endowments, such as natural resources, geographical location, labour, etc. Also, advantages in the investment environment include economic systems and political, laws, regulations and policies, market capacity, infrastructure, and community factors. The OLI paradigm holds that FDI is related to the host country's location advantages and is consistent with MNCs' strategic objectives.

1.4 Hypothesis

The reason behind Alibaba choosing Indonesia to expand its market is because of location advantages divided into four factors: economic systems and political, regulations and policies, infrastructure, and community factors. Indonesia's e-commerce market is considered capable of providing fantastic opportunities, both for companies' benefit and their prospects for future development.

1.5 Research Purpose

1. This study aims to enrich the study of subjects related to the title.
2. This study aims to apply the theories that have been obtained and studied for several semesters in International Relations courses.

3. This study aims to determine and answer why alibaba chose the Indonesian e-commerce market as an investment expansion.
4. Analyzing the investment process made by Alibaba to e-commerce in Indonesia.

1.6 Research methodology

This research would implement the qualitative research methodology as the method to analyze the researcher's curiosity about the case. The qualitative techniques use collecting data and information obtained from journal articles, an official online source, books, a scientist's point of view, trusted document through an online source, and other sources relevant to the author's research. The researcher will analyze the meaning and gain a holistic view of a phenomenon and describe the importance of a phenomenon from the researcher's perspective and understanding.

1.7 Scope Research

From the various possibilities and factors that underlie Alibaba's investment in the Indonesian e-commerce market, this study will limit the analysis to 4-factor studies. Namely, economic factors, political factors, technological factors, and the social factors that Indonesia has to attract Alibaba to make it a destination for expanding its e-commerce market.

Since the topic of this study is relatively new, explicit time constraints are required. Therefore, the author limits the period from 2014-2018, when Alibaba decided to inject several investment funds into Tokopedia. This time limitation is appropriate because when a company chooses to invest, it must have various reasons that have been previously considered and analyzed.

1.8 Outline

This research will be divided into four continuous chapters. The chapters are divided:

Chapter I: introduction

This chapter explains the background of the problem, which is an exploration of the research title, identification of issues that discuss the research problem's basis, then proceeding with the research's objectives and uses, the framework for analysis, research methods, and data collection techniques—closed with systematic writing.

Chapter II: Alibaba as a Global E-Commerce Company Leader.

This chapter is divided into three parts. The first part will explain the trends in the development of e-commerce in the world. The second part will focus on a general description of the e-commerce company Alibaba Group Holding Ltd. The third part will discuss the development of Alibaba Group Holding Ltd in the domestic and international market. The fourth part will discuss the history of Alibaba Group's business expansion in Indonesia, namely Lazada and Tokopedia.

Chapter III: The reasons why Alibaba entered the e-Commerce market in Indonesia.

The analysis in chapter three is divided into four sub-chapters. Namely, research related to economic factors, analysis of political factors, analysis of technology and internet factors, and the last sub-chapter describes the study of community factors.

Chapter IV: the conclusion

The last chapter presents the conclusions from the analysis that has been carried out in the previous chapters, which is also the answer to the research questions.