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Does money buy friends? the effect of economic interdependence between China and Indonesia on the Natuna territorial dispute

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Master's Thesis

Does money buy friends?

the effect of economic interdependence between China and Indonesia on the Natuna territorial dispute

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Abbreviations

APEC = Asia-Pacific Economic Cooperation

ASEAN = Association of Southeast Asian Nations

BRI = Belt and Road Initiative

CAMEO = Conflict and Mediation Event Observations

EEZ = Exclusive Economic Zone

FDI = Foreign direct investment

FPI = Foreign portfolio investment

GDP = Gross national product

MSRI = Maritime Silk Road Initiative

ICEWS = Integrated Crisis Early Warning System

SEA = South East Asia

UN = United Nations

UNCLOS = United Nations Convention on the Law of the Sea

US = United States

USD = United States Dollar

Introduction

South East Asia (SEA) has been identified as the region in the world where the US-China rivalry is most intense. Therefore, both China and the US have tried to deepen their relationships with this region. China has mainly done this by improving its economic relations with the region through trade and investment (Ferchen, 2022; Shambaugh, 2018). However, the question is whether this charm offence has actually improved China's relations with SEA, as countries in the region are known to be wary of great powers (Kamaruddin, 2021). This is a valid question as several studies have pointed to the generally positive effects of increasing economic exchange on political relationships between states (see for instance Gartzke & Li, 2003; Lee & McLaughlin Mitchell, 2012).

One of the SEA countries that has had a strained relationship with China in the past is Indonesia. Their foreign relations were amicable until 1967. In that year, president Suharto came to power and the diplomatic relations were broken off (Anwar, 2019, p. 2). This was because China was accused of supporting the alleged coup of the Indonesian Communist Party in 1965. Diplomatic relations were restored in 1990, but only became started to improve when Suharto left office in 1998 (Gammeltoft & Tarmidi, 2013, p. 147). In 2005, the countries signed a Strategic Partnership Agreement when the Chinese president visited Indonesia. In this agreement they agreed to cooperate in several areas like security and the economy (Priyandita, 2019). For the past two decades Indonesia has developed strong economic ties with China (Hamilton-Hart & McRae, 2015). Currently, China is Indonesia's largest trading partner and second largest investor (Fitriani, 2021, p. 196). However, there are also still several conflicts between the two states. The most important is the Natuna territorial dispute that started in the early nineties (Fitriani, 2021). Another important issue is the treatment of the Chinese minority in Indonesia. The animosity between the ethnic Chinese and indigenous Indonesians started in colonial times when the Dutch regarded the ethnic Chinese as second class citizens but the indigenous population as third class citizens (Koesoemawiria, 2021a). The Chinese Indonesians have faced discrimination and racism ever since, especially after the communist coup attempt in 1965 (Koesoemawiria, 2021b). Other important issues are growing concerns about the growing economic influence of China in Indonesia and the treatment of the Uyghur Muslims in China, given that Indonesia's majority is Muslim (Rakhmat & Aryansyah, 2020).

This history makes Indonesia an interesting case to see if China's improved economic relations in SEA have actually led to better political relationships in the region. The island nation has a long history of non-alignment. Therefore, it does not have a clear side in the US-China rivalry. Not only is the relationship between Indonesia and China an interesting case study, it is also worth studying in its own right. Indonesia is the largest and most populous country of SEA. Indonesia is rapidly becoming an important player in the world as it is estimated to become the seventh-largest economy in 2030 (Oberman et al., 2012). China has also considered it the gateway to South-East Asia and therefore an integral part of the Belt and Road Initiative (Negara & Suryadinata, 2019, p. 65; Yuen Yee, 2021). Indonesia has been seeking to position itself as a great power in the Indo-Pacific region (Shekhar, 2018). However, its economically and military capabilities are still relatively weak. In contrast to other emerging powers, Indonesia has gained regional leadership legitimacy through democratization and regional engagement. It has played a significant role as a mediator in regional conflicts (Acharya, 2015, pp. 1–2). In short, Indonesia is an important and well-respected regional power in SEA and an emerging power on the world stage. Therefore, understanding the relationship between China and Indonesia is important in world politics. Following from this, this thesis will focus on the following research question:

“How has the development of the economic interdependence between China and Indonesia affected their behavior in the Natuna territorial dispute?”

This thesis will focus on the effect of economic interdependence on how the Chinese and Indonesian government handle the Natuna territorial dispute. There are several reasons for focusing on the Natuna dispute. Firstly, it is the largest long-term issue between China and Indonesia. The way they manage this dispute can show us whether economic relations can improve conflicts between them. Secondly, the dispute started in 1992, when China and Indonesia were barely economically interdependent. Therefore, it is possible to analyze the dispute over time and see if the increasing economic interdependence has an effect. Thirdly, a quantitative study by Lee & McLaughlin Mitchell (2012) suggests that economic interdependence can have a positive effect on the management of territorial disputes. They showed that high bilateral FDI flows decreases the chance of high-level escalation and increases the chance of peaceful management.

This thesis consists of six chapters. The next chapter presents a review of relevant literature in order to point out why the research question of this thesis is relevant. The second chapter discusses the theoretical framework of this thesis, which is based on modern commercial liberalism, the school that is currently dominant among scholars studying this field. Next, the third chapter discusses the methodology of this thesis. The fourth chapter describes the development of the economic relationship between Indonesia and China from 1990 until 2020 on basis of three indicators: trade, foreign direct investments and external debts. At the end of this chapter, the hypotheses of this thesis are presented. Chapter 5 critically analyzes the Natuna dispute with the use of the theoretical framework. At last, there will be a short conclusion.

1. Literature review

This chapter aims to critically assess the current literature about Chinese investments in Indonesia. This chapter first discusses the relatively small amount of literature dedicated to the political and economic relationship between Indonesia and China. Then, it moves on to the scholarship that focuses on the MSRI in South East Asia, because this is a much larger body of literature. The conclusion will point out that the research question of this thesis fills a gap in the literature.

There is only a small body of literature that investigates the political and economic relationship between China and Indonesia. These works have given a historic account of the tumultuous relationship (Fitriani, 2018, 2021; Hamilton-Hart & McRae, 2015; Priyandita, 2019). Moreover, they describe the foreign policy that Indonesia has had toward China. Priyandita (2019) has evaluated their strategic partnership and Hamilton-Hart & McRae (2015) have described Indonesia's strategy to not form any alliances (Fitriani, 2018). Anwar (2019) and (Laksmiana, 2011) explain the bilateral relationship between China and Indonesia. Although they do discuss the growing economic relations between the countries, they argue that the bilateral relationship is mainly shaped by domestic factors, like the perceptions of Indonesians and Indonesian domestic politics. While these are indeed important factors, there are also several studies that have pointed to the generally positive effects of increasing economic exchange on political relationships between states (see for instance Gartzke & Li, 2003; Lee & McLaughlin Mitchell, 2012). This different perspective could shed a new light on factors that influence the political relationship between China and Indonesia.

While there is only a small body of literature dedicated to the bilateral relationship between Indonesia and China, there is a huge body of literature focused on Chinese investments in the region of Southeast Asia (SEA) as a whole. Moreover, most researchers have specifically focused on the Maritime Silk Road Initiative (MSRI), a part of the Belt and Road Initiative (BRI). The BRI was launched in 2013 and is a global development strategy with a focus on infrastructure. The aim is to develop new trade routes connecting China and the world. Therefore, China invests in foreign transport and energy infrastructure in two main routes: one over sea and the other over land (Huang, 2016). The BRI is still expanding and involves more than 130 countries across the world. It is mainly funded by Chinese policy banks and state-owned commercial banks (Coenen et al., 2021, p. 3). However, Gong (2018) has pointed out that it is hard to tell which investment projects are part of the MSRI and which are not. Moreover, he also notes that the MSRI did not have a significant effect. Even before the MSRI was launched in 2013, China and SEA were already intensifying their economic relations. Therefore, it is better to view the MSRI as a normal continuation of intensifying economic relations.

Descriptive works have mainly focused on the size of Chinese investments in the region, how Chinese investors deal with SEA's institutional environment and what actors are involved (Gammeltoft & Tarmidi, 2013; Gong, 2018; Oh, 2017; Suleiman, 2019). Scholars have also been successful in identifying why China and SEA are taking part in this project. SEA, including Indonesia, is mainly interested in economic gains. They hope that Chinese investments in the region will boost their economies (Blanchard, 2018; Ganesan, 2018; Salim & Negara, 2016; Sjöholm, 2013). The economic gains could indeed be huge, especially considering the opportunities to secure investments and know-how and to improve infrastructure (Yu, 2017). Overall, scholars also agree that China is interested in SEA for the economic gains. MSRI is an opportunity for China to increase exports, access new markets and increase resource security (Andrews-Speed, 2015; Blanchard, 2018; Negara & Suryadinata, 2019; Shi & Yao, 2019; Sjöholm, 2013). Most scholars agree that China has also made efforts to improve relations with SEA and strengthen its strategic position there since the post-Cold war era (Gong, 2018, pp. 637–638). In short, the scholarship on investments in SEA has been successful in describing the development and in identifying the motives of the countries involved.

Scholars have also been successful in indicating factors that will determine the success of the MSRI. Firstly, several scholars have noted that the success of the project in SEA will depend on China's capabilities to successfully implement it (Blanchard, 2018; Gong, 2018). There are signs that there are problems with coordination that lead to a lack of cohesiveness that is confusing for China's partners. Another important factor is being able to secure funding for the project. Rillo & Ali (2017) have, for instance, pointed out that it has proven difficult to obtain private funding. There are also external factors at play. The success of the projects also depends on how SEA countries respond to the MSRI. This is a valid concern as there are trust issues between SEA and China. SEA fears the rising military capabilities of China and the border issues in the South China Sea (Yu, 2017). There was a study from Chen (2017) that identified what factors lead to hostile reactions to the MSRI in SEA. Blanchard (2018) has specifically noted that in the case of Indonesia, internal political tension is an important factor (339). The last factor that has been discussed is the counter-initiatives that other powers in the region, like India, Japan and the US, could potentially launch (Gong, 2018).

The current debate in the literature is about the effects of these rising investments. Notably, there is a considerable amount of literature dedicated to the effects of the MSRI on human rights, sustainable development goals and the environment (Frost, 2006; Frost & Ho, 2005; Gallagher et al., 2021; Renwick et al., 2018). There is a heated debate about the effect of the MSRI on the political situation in SEA and its regional order. There is one group of scholars that only focuses on China's economic influence in the region and considers the MSRI's effect on the regional order insignificant (Cai, 2017; Djankov, 2016; Ikenberry & Lim, 2017; Shambaugh, 2018; Wang, 2016). A second group of scholars criticizes the MSRI for lacking cohesiveness and sufficient financial means (Cooley, 2015; Lam, 2017; Landry, 2018). Therefore, they think China will probably not make true what it set out to do. Eventually, the costs will outweigh the benefits. At last, there is a group that is significantly more positive. They think the MSRI will be a successful means for China to change the political order in Asia. The MSRI is set to promote Chinese values and interests. Moreover, the MSRI will successfully lead to a better strategic position in the region (Blanchard, 2017; Brewster, 2017; Kuik, 2015; Ntousas, 2016). However, it has to be noted that most views are still speculative. They are too broad and there is still a lack of empirical evidence (Blanchard, 2018; Gong, 2018; Zeng, 2021). (Blanchard, 2021) specifically points out there is a lack of more in-depth research that focuses on specific industries, regions, or countries. An in-depth case study on the political effects of the economic relationship between Indonesia and China would address this gap in the literature.

In conclusion, the aim of this thesis is to analyze how the growing economic relationship between Indonesia and China has affected their political relationship, specifically one of their largest disputes, the Natuna territorial conflict. This addresses two gaps in the literature. First of all, this thesis adds to the scholarship focused on the bilateral relationship between Indonesia and China by being the first to focus on the political effects of economic factors rather than domestic factors. Moreover, this thesis also adds to the scholarship on the MSRI in SEA by empirically researching the political effects of investments in a specific country.

2. Theoretical framework

This thesis presents a short overview of theories that have engaged with the relationship between trade or economic interdependence and conflict, specifically focusing on territorial disputes. The debate on the effect of trade on war at least goes back for centuries to enlightenment scholars like Kant and Montesquieu. (Gartzke et al., 2001, p. 391; Walker & Rousseau, 2016, p. 24; Zeng, 2020b, p. 1). This chapter discusses the contemporary contributions to the field. These have mainly been under the name of Commercial Liberalism¹ (the part of liberalism that focuses on the effects of trade), but have drawn from several theoretical approaches (Gartzke & Zhang, 2015). In the last decade, modern commercial liberalism has advanced its theories by proposing three main causal mechanisms. These are the mechanisms that scholars are currently attempting to finetune and find empirical support for (Chang & Kastner, 2017; Gartzke & Zhang, 2015). This chapter critically reviews these three causal mechanisms, although the work on the inform mechanism has been fragmented and contradictory that it has been split up in two.

2.1 The constraint mechanism

The first causal mechanism claims that trade constraints countries to start conflict or let it escalate. The reason for this is that war and other high conflict situations disrupt trade. Therefore, increasing economic interdependence constrains countries to start conflicts. This also theorizes that economic sanctions are less likely to occur because these would be costly (Polachek & Xiang, 2010). It has also been noted that domestic actors will lobby at their government for de-escalation to protect their economic interests (Gartzke & Zhang, 2015, p. 430). However, the main issue with this proposed mechanism is that scholars do not agree on which actions are costly enough for countries to avoid and which actions are not (Zhang, 2018, p. 28). Moreover, it has also been argued that the costs of war are already high and therefore the potential loss of trade must be substantial to have an effect (Gartzke & Westerwinter, 2016, p. 326).

Firstly, it is important to look at it more nuanced than merely looking at trade. There are also other ways countries can be economically interdependent. The most important being overseas investments and debts (Gartzke & Zhang, 2015). The important difference between these two indicators and trade is that they are asymmetrical. If conflict would disturb overseas investments and loan provision, this is mostly costly for the country receiving investments or debts. Moreover, an escalation of conflict could hurt the relationship between the countries. This could lead to the country that gives out debts or investments to make the terms of the agreements less favorable for the other country. Therefore, the debtor/investor has more power in the relationship. While a country receiving investments or loans could be constrained to let a conflict escalate, this is not the case for the opposing party. Secondly, it is important to take into account that this causal mechanism is not equally strong for all countries. This depends on how important the economic relationship with the other party is for the total economy and the total sizes of both economies. If the share of investments/trade/debt is only small, this means it is less important for the concerned country, even if the absolute amount is large. Here it is crucial to take into account the total sizes of the economies and how they compare to each other. If the countries are of unequal size, this means that their dependency on the economic relations with the other country is different. This is the case for all types of economic relations, but especially interesting regarding trade. As opposed to loans and investments, trade creates more of an equal dependency. However, if the economy of one country is significantly larger than the other, this means that they are not equally dependent on this trade. The same amount of trade can be only a small share of total trade for one country but a large share for another country. This means that trade can also create unequal

¹ sometimes also called commercial peace theory

dependencies. This then translates in one country being more affected by the trade constraints mechanism than the other. It is also important to not view countries as unitary actors. Within a country there are several domestic actors active with different personal interests. This means that some actors might be affected by the trade constraints mechanism, while others are not. Another criticism is that the theory does not go into the question of whether the territory that is disputed is economically valuable itself. In that case, there are two economic interests opposing each other. On the one hand, conflict and economic sanctions could be costly. While on the other hand, they could also lead to economic gains. This is important to take into consideration. At last, the theory only focusses on the constraining effects of high-level conflict. It would have to be assessed what kind of conflict would (potentially) disrupt economic activities and which would not.

2.2 The transform mechanism

The second causal mechanism is that economic interdependence can transform the interests of states. This causal mechanism is fundamentally different from the other two. It theorizes that instead of trade changing the behavior of states it changes the interests of states (Gartzke & Zhang, 2015, p. 432). The first argument is that trade or FDI makes it less interesting for countries to rely on conflict to realize their goals (Zhang, 2018, p. 30). They can obtain resources through trade and are therefore less reliant on territory. This theory claims that gains from trade and FDI can substitute gains from territory, for instance investing in the development of an area instead of owning it yourself through capturing land (Brooks, 2007; Chang & Kastner, 2017; Gartzke, 2007; Lee & McLaughlin Mitchell, 2012). Secondly, this mechanism theorizes that increasing economic interdependence will lead to converging interests of countries (Gartzke et al., 2001, p. 395). One of the most important examples of cases where economic interdependence led to converging foreign policy goals is the economic integration of the European Union countries (Lee & McLaughlin Mitchell, 2012, p. 682). The main criticism of this causal mechanism is that it is not nuanced. It is not discussed which specific actors would be involved in this process and how their specific interests would be transformed. Specific case studies would be necessary to further investigate this.

2.3 The regular inform mechanism

The third causal mechanism is that trade informs. It is often said that war is the result of a bargaining failure caused by a lack of information about the opponent. Both countries underestimate each other's commitment because they are not able to assess each other's resolve and capabilities. The main reason for this is that countries are not able to communicate credibly, meaning they are not able to express how serious they are about an issue. Rather, they bluff and rely on "cheap talk" (Gartzke & Li, 2003, p. 562; Morrow, 1999; Powell, 2002). The main idea of this causal mechanism is that economic interdependence creates more mutual understanding and it will allow countries to communicate better. Economic interdependence creates a wider bargaining range, because countries have more methods to communicate, like economic sanctions. Economic sanctions are a way of saying they are serious about an issue without seriously letting a conflict escalate. It is a middle step in conflict that is (relatively) peaceful and credible (Gartzke & Zhang, 2015). Economic sanctions fall under a method of "costly signaling." These are signals that states use to communicate, but specifically signals that are costly. This way states show that they are serious (Gartzke & Li, 2003; Xu et al., 2012; Zeng, 2020a). There are two strategies to do this (Fearon, 1997). The first strategy is sinking costs, for instance mobilizing forces (Slantchev, 2005, 2011). This action is costly in itself. Secondly, there is the strategy of tying hands, for instance economic sanctions. This means that states threaten to perform an action that will be costly for them, like threatening with economic sanctions (Sartori, 2002). Zeng (2020) and Dafoe & Kelsey (2014) have mentioned another reason why costly signaling reduces conflict escalation. Actions like economic sanctions are not only costly for the country that initiates them, but also for the

country that undergoes them. Therefore, the country that receives a threat of economic sanctions is more likely to concede to avoid costs.

There are several points of critique on this mechanism. The first is that a lack of understanding is not always the root of an issue. If two countries have diverging interests and they are both completely resolved, mutual understanding might let the conflict escalate. If a country is purposefully vague about its intentions and resolve, this might continue to put pressure on the other party without letting the situation escalate. The other country might react more serious if it knew how serious the opposing party is. The second critique is that it is important to consider the differences between economic sanctions and military mobilization. It is not taken into consideration that trust is important in the economy and in business. If a country uses economic sanctions this can signal to the opposing country that it is an unreliable business partner. This could potentially hurt the reputation of a country to such a degree that other countries also consider it to be an unreliable business partner. Therefore, the long-term costs of economic sanctions could be higher than the mechanism proposes. It is also important to point out that while economic sanctions are mainly costly for specific sectors of the economy, military sanctions are only directly costly for the national government. Therefore, economic sanctions are a less popular measure than military mobilization. The last critique on the regular inform mechanism is that it does not take into account asymmetric economic relations. This point is addressed in an alternative version of the mechanism, which is discussed in the next section.

2.4 The alternative inform mechanism

Some authors have taken into account the asymmetry of trade relations when theorizing this mechanism (Barbieri, 1996; Zeng, 2020a, p. 635). This alternative mechanism is contradictory to the regular inform mechanism. These authors claim that the country who is the less dependent one in the relationship will have more incentive to exploit the vulnerabilities of the more dependent country. Therefore, the relatively independent country will be more inclined to bluff, i.e. to make claims on things they are not willing to fight for. However, this will downgrade the seriousness of the threat. This means that the relatively dependent country will also be more inclined to resist more.

2.3 The approach of this thesis

This chapter critically assessed four causal mechanisms of how economic interdependence can influence territorial disputes that are prominent in the current literature. However, these mechanisms are also critiqued. This thesis will test these mechanisms, however, with taking into account asymmetrical economic relations, different types of economic relations, and different domestic actors and the potential economic gains from disputed areas.

3. Methodology

This section outlines the methodology of this thesis. It first discusses how the independent variable, economic interdependence was operationalized and how data was collected. Then, the chapter discusses the operationalization and data-collection of the dependent variable, which is the behavior of Indonesia and China in the Natuna dispute.

3.1 Measuring economic interdependence

The independent variable of this study is the economic interdependence between China and Indonesia. There is a focus on analyzing the how this relationship developed in the last thirty years and how important these economic ties were for the respective countries, in order to investigate economic dependency. The aim was to collect data from the period 1990 until 2021. However, this was not always possible for all indicators. Moreover, data for 2021 was not available for any indicator.

Economic interdependence was measured through three indicators: trade relations, foreign direct investments (FDIs) and external debt. These are the three most common indicators to measure economic interdependence between countries (Gartzke & Zhang, 2015). Therefore, these are also the indicators on which the most data is available. Another important indicator is foreign portfolio investments (FPI). FDI and FPI are the most common ways for overseas investments (Picardo, 2021). However, unfortunately there was not sufficient data available to include this indicator in the study.

Additional to taking into account the economic interdependence, this study also paid attention to the difference in size between the economies of China and Indonesia. This was done by looking at their GDP and GDP per capita with data from the World Bank.

3.1.2 Measuring trade relations

The data that was used to measure trade relations was retrieved from the statistical portal of the Asia-Pacific Economic Cooperation (APEC). This database facilitates detailed analysis of bilateral trade flows between countries in the Asia-Pacific region. Data was available from 1990 until 2020. The study includes data about import and export of merchandise goods between Indonesia and China. Not only in absolute terms, but also as percentages of their total import and export. This was to see if how dependent they are on each other. Moreover, this thesis discusses what their most traded items were, to see if there were any substantial differences between the two countries. Unfortunately there was no data available on bilateral trade in commercial services.

3.1.3 Measuring foreign direct investments

In contrast to trade relations, it was more difficult to find data about the FDIs between China and Indonesia. Most data about this topic was not publicly available. Therefore, this thesis mainly had to rely on the data that was presented in scholarly articles (but was not publicly available). There were several disadvantages of this. Firstly, there was no study that studied the entire period from 1990 until 2020. Therefore, different studies had to be combined. Secondly, all authors had slightly different ways of measuring FDI and are therefore hard to compare. Thirdly, most authors did not include their entire data sets, but rather provided graphs and mentioned some numbers in their text. Despite these hurdles, it was possible to collect sufficient data to show the general development trends about Chinese FDIs in Indonesia from 1990 until 2020. This is sufficient for the purpose of this study. However, there was no data available on Indonesian FDIs in China, as this topic does not receive scholarly attention nor is it included in articles about Chinese FDIs in Indonesia. This is not too problematic, as the reason it does not receive scholarly attention is because it is probably not a significant amount.

3.1.4 Measuring external debt

Out of all three indicators, it was the most difficult to collect data on external debt. This study had to rely newspaper articles and on a single scholarly study that provides a graph of the development of external debt over a longer period of time. Unfortunately this period was only from 2008 until 2017.

3.2 Measuring conflict in the Natuna territorial dispute

The dependent variable of this thesis is the amount of conflict and behavior of the governments of China and Indonesia in the Natuna territorial dispute. This was done by qualitatively analyzing the development of the dispute since its inception in 1992 until 2021. We looked at the number of incidents that occurred and the level of hostility regarding the event. This included any type of incident that was related to the dispute, including but definitely not limited to military action, economic sanctions and statements from governments. High-level conflict in the dispute is characterized by a large amount of incidents regarding the dispute (this can be any type of incident) and low-level conflict in the dispute can be characterized by a low amount of incidents regarding the dispute. Next, for measuring the level of hostility of the events the (CAMEO Conflict and Mediation Event Observations) coding system was used. This is a popular system⁰ also used for instance in the Integrated Crisis Early Warning System (ICEWS) which tries to gather data about political events to have early indications of the development of a political conflict. It has also been used by scholars to measure the level of conflict or hostility between countries (see for instance Zeng, 2021). This scaling system is used to quantitatively assess the hostility or cooperation level of events. It ranges from -10 to 10, where negative numbers are regarded hostile and positive numbers are regarded cooperative. Neutral events are rated with zero. The most hostile events are rated with -10 and the most cooperative events are rated with 10. The CAMEO system is suitable for this study because it assesses the severity of incidents ranging from high cooperation up until high hostility. In contrast, there is an emphasis in the literature on measuring high level conflict (Braithwaite & Lemke, 2011). There are two characteristics of the CAMEO scale that had to be adjusted for this study. The first is that the scale is not only meant for assessing territorial disputes, but also many other types of political events. Therefore, this study works with a selection of the events included in the CAMEO scale that are applicable for this case. Secondly, the scale is a quantitative measurement while this study is qualitative. This means that the scale is used differently than was intended. The scale is meant for coding events, but here it is used as a aiding tool in a qualitative study. The quantitative scale is merely used to rate events from most cooperating to most hostile. Table 1 shows the types of events from CAMEO included in this study. The quantitative scaling is included to give a sense of how the types of events compare to each other.

Information about the Natuna dispute was mainly gathered from newspaper articles, government statements and some scholarly articles. The main newspapers that have been closely following the dispute are The Straits Times and The Diplomat. It was the hardest to find information about the start and the first ten years of the dispute. Information from this time period was mainly gathered from a scholarly article that thoroughly describe the development of the dispute.

Table 1: CAMEO scale with incidents in territorial disputes (based on Schrodt, 2021)

| Type | Value range | Event |
|------------------|-------------|--|
| High cooperation | ≥7 | [9.0] Demobilize armed forces [9.0] De-escalate military engagement [9.0] Declare truce, ceasefire [7.0] Express intent to accept mediation [7.0] Apologize [7.0] Forgive |

| | | |
|--------------------|--------------------|---|
| | | [7.0] Ease economic sanctions, boycott, embargo |
| Median cooperation | ≥ 5 & < 7 | [6.4] Cooperate economically [5.0] Express intent to settle dispute |
| Low cooperation | > 0 & < 5 | [3.4] Praise or endorse [3.5] Engage in diplomatic cooperation [3.5] Defend verbally [4.0] Appeal to others to meet or negotiate, settle dispute or engage in mediation [4.0] Express intent to meet or negotiate [4.0] Express intent to cooperate, not specified below |
| Low hostility | > -4 & < 0 | [-2.0] Investigate crime, corruption [-2.0] Investigate military action [-2.0] disapprove, criticize or denounce [-2.0] Accuse e.g. of crime, corruption, aggression. [-2.0] Complain officially [-2.0] Bring lawsuit against [-4.0] Reduce or break diplomatic relations |
| Median hostility | > -8 & ≤ -4 | [-5.0] Demand mediation [-5.0] Demand withdrawal [-5.0] Demand meeting, negotiation [-5.0] Reject proposal to meet, discuss, or negotiate, mediation [-5.0] Defy norms, law [-5.0] Reject accusation, deny responsibility [-5.6] Reduce or stop economic assistance or aid [-5.8] Threaten non-force, e.g. boycott, embargo, sanction, to reduce or break relations, halt negotiations/mediations [-6.5] Halt negotiations [-7.0] Halt mediation [-7.0] Threaten with violent repression [-7.0] Threaten to use military force .e.g. blockade, occupation [-7.2] Demonstrate military or police power [-7.2] Increase police alert status [-7.2] Increase military alert status [-7.2] Mobilize or increase police power [-7.2] Mobilize or increase armed forces [-8.0] Impose embargo, boycott, or sanctions |
| High hostility | ≤ -8 | [-9.5] Impose blockade, restrict movement [-9.5] Occupy territory |

4. The economic interdependence between China and Indonesia

This chapter discusses the independent variable of this thesis, namely, the economic interdependence between China and Indonesia. This thesis uses three indicators to measure economic interdependence: trade, foreign direct investment (FDI) and external debts. However, first it is important to shortly look at the difference in size between the economies of China and Indonesia.

In 2021, China had a population of 1.4126 billion, while Indonesia had a 275.1 million inhabitants. While Indonesia is still the 4th country with the largest population, China's population is still about five times the size as Indonesia's (World Bank, 2021). In 1990, China's total GDP was about 3.5 times larger than Indonesia's (see figure 1). This means that the GDP per capita of Indonesia was more than twice the size of China's. However, China's economy started to grow rapidly and in 1998 China's GDP per capita surpassed Indonesia (see figure 2). The gap between the two economies has continued to grow. There was only a small slowdown in China's economy around 2014-2015. In 2020, China's GDP was about 14 times the size of Indonesia's economy. It is important to realize the difference in size between the Indonesian and Chinese economies, because this means that trade between the two countries has most likely developed asymmetrically. It is likely that the bilateral trade between the two countries is more significant for the Indonesian economy than for the Chinese economy.

Figure 1 (Data from World Bank "World Development Indicators Database – GDP")

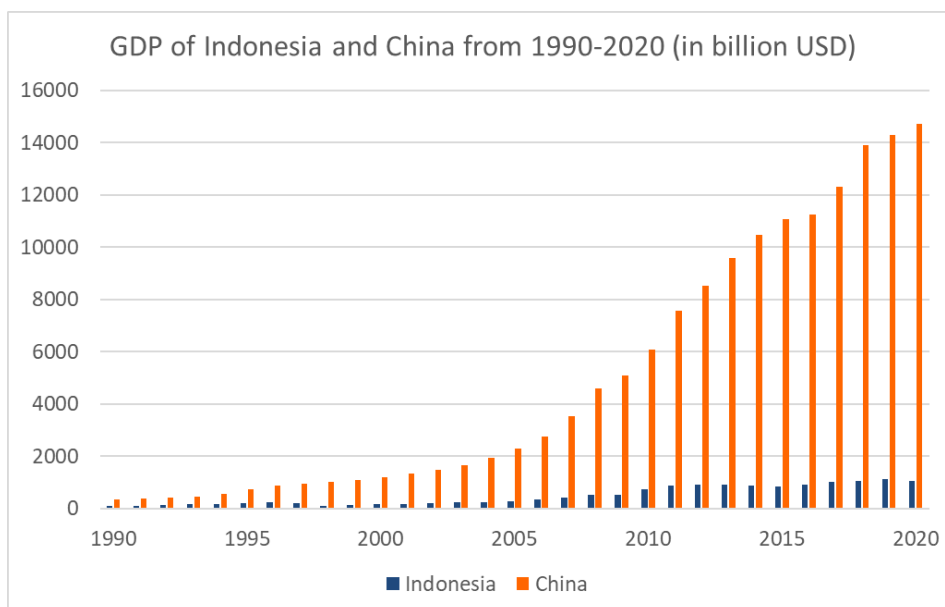
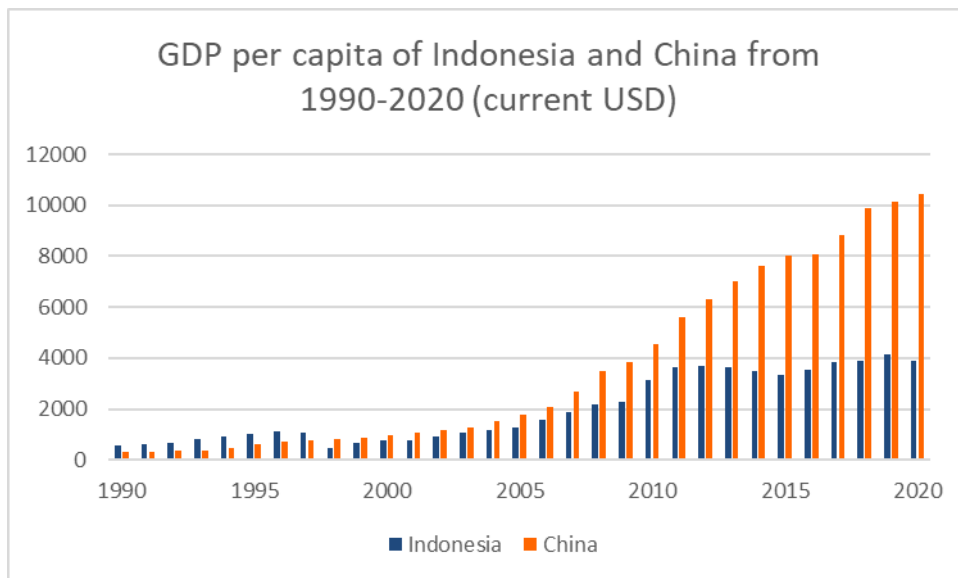


Figure 2 (Data from World Bank “World Development Indicators Database – GDP per capita”)



4.1 Trade relations

The trade relations between Indonesia and China in the last 30 years can mainly be characterized by quick and asymmetric growth since the turn of the century (see figure 3). The Free Trade Agreement that ASEAN and China signed in 2002 has played a positive role in stimulating trade (Gammeltoft & Tarmidi, 2013, p. 148). There was only a small dip from 2013 until 2015, which coincides with an overall slowdown of the Chinese economy. In 2020, the total trade between the two countries was 71410 million US dollar.

At first, Indonesia had a small trade surplus. However, since 2008, it has had a trade deficit. This has mainly been due a growing amount of Chinese imports (see figure 4). Indonesia mainly exports lignite, coal briquettes, palm oil, sulfate chemical wood pulp and ferroalloys to China. These are all raw materials (Putra, 2020). China’s largest export products to Indonesia are electronics like telephones, broadcasting equipment and computers (The Observatory of Economic Complexity, 2020).

Since 2013, China is Indonesia’s largest trading partner (surpassing Japan). In 1990, China accounted for 3 percent of Indonesia’s export destinations. This has steadily increased until 19 percent in 2020 (see figure 5). Regarding imports, China is even more important for Indonesia. In 1990, 3 percent of imports in Indonesia came from China. This has steadily increased until 28 percent in 2020 (see figure 6).

In contrast, Indonesia is only a minor trade partner of China. The Indonesian share of the total Chinese imports has between 1 and 2 percent in the last 30 years, without a clear growth. The Indonesian share of the total Chinese exports peaked in 2019 with 1.9 percent (APEC Statistics).

It could be argued that China is dependent on Indonesia for resources. However, this is not the case. One of Indonesia’s most valuable resources is nickel ore, which is an important material for building electric cars. However, currently only 7.74 percent of China’s nickel ore imports originate from Indonesia. In contrast, almost 90 percent of Indonesia’s nickel ore exports go to China (Sanjaya, 2022).

Figure 3 (Data from APEC Statistics “Bilateral Linkage Database – Trade Flows”)

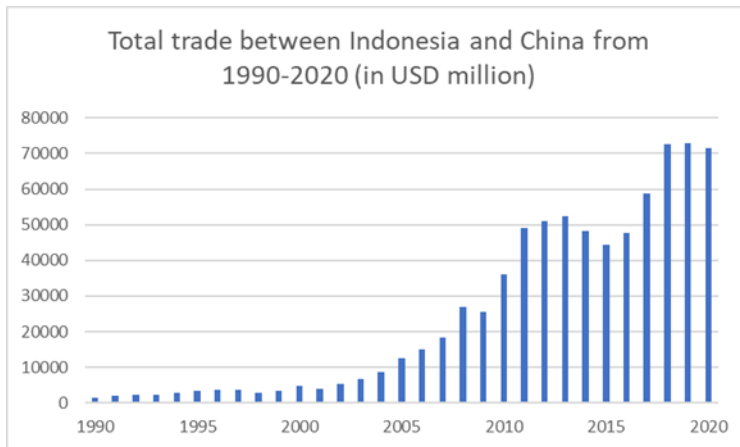


Figure 4 (Data from APEC Statistics “Bilateral Linkage Database – Trade Flows”)



Figure 5 (Data from APEC Statistics “Bilateral Linkage Database – Trade Flows”)

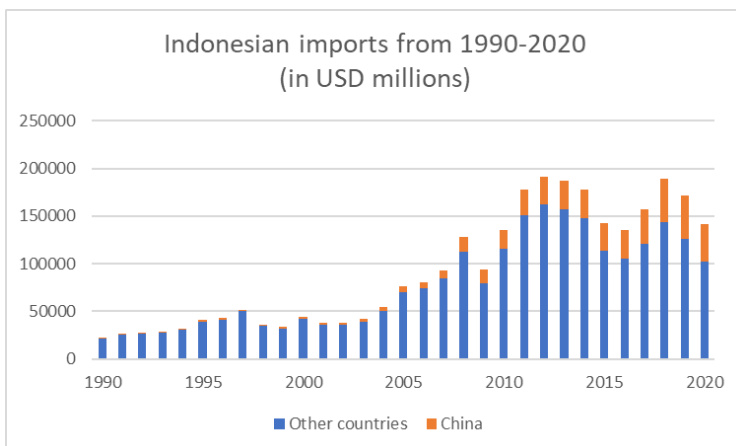
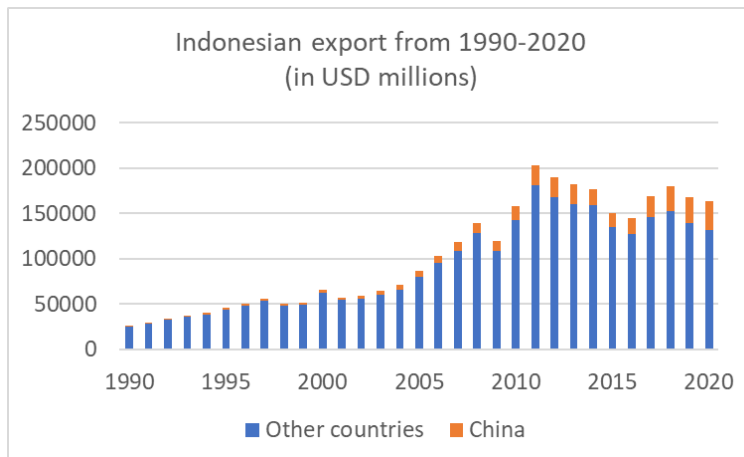


Figure 6 (Data from APEC Statistics “Bilateral Linkage Database – Trade Flows”)



4.2 Foreign direct investments

Foreign direct investment (FDI) is an “investment by a company incorporated in one country into productive assets in another country with the aim of exerting control and reflecting a lasting interest” (Gammeltoft & Tarmidi, 2013, p. 138). The main characteristic of the FDI between Indonesia and China is a rapid growth of realized Chinese FDI in Indonesia since 2009, except for a dip from 2013 until 2015. There is no data available about Indonesian FDI in China, but this is most likely due to its insignificant size.

An article by Gammeltoft & Tarmidi (2013) was the first comprehensive account of FDI flows from China to China. They focus on the early period. According to them, the first Chinese FDI recorded by the Indonesian government is a single project in 1995 (1). However, the amount of FDI’s only became significant after 2000 (156). In this period, Chinese FDI’s developed from occasional, isolated projects to a more systematic approach. In 2008, China had become the tenth largest foreign investor in Indonesia (137).

Negara & Suryadinata (2019) provide data that show the long-term development of Chinese FDI in Indonesia (see figure 8). Besides a dip in 2015, Chinese FDI’s have increased significantly, especially since 2013. This is also the year that Indonesia joined the MSRI. In 2015, China surpassed the United States and is now the second largest investor in Indonesia. Figure 7 shows that in the period from 2010 until 2017 the large majority of projects was realized in the metal, machinery and electronics sector. Data from Statista show the total stock of FDI from China to Indonesia between 2010 until 2020. This shows us that also after 2017, the amount of FDI is increasing (see figure 9).

Figure 7: Cumulative Chinese realized FDI in Indonesia by sector, 2010-17 (in USD million) (Negara & Suryadinata, 2019, p. 8)

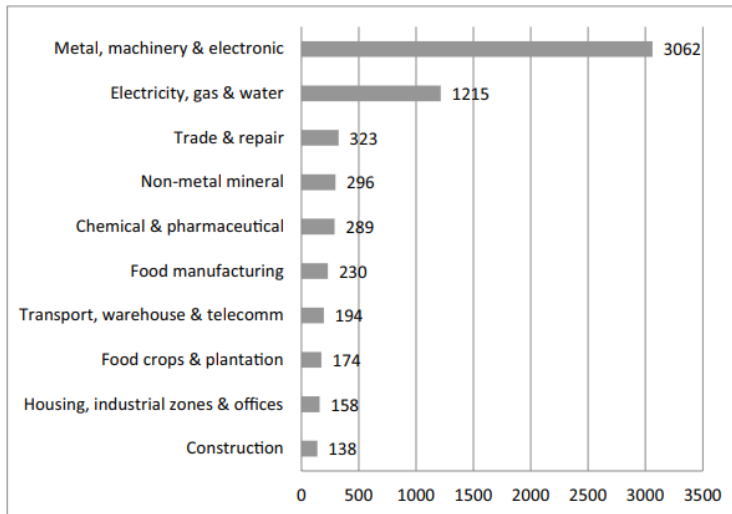


Figure 8: Realized FDI in Indonesia from three major countries (in USD million)(Negara & Suryadinata, 2019, p. 7)

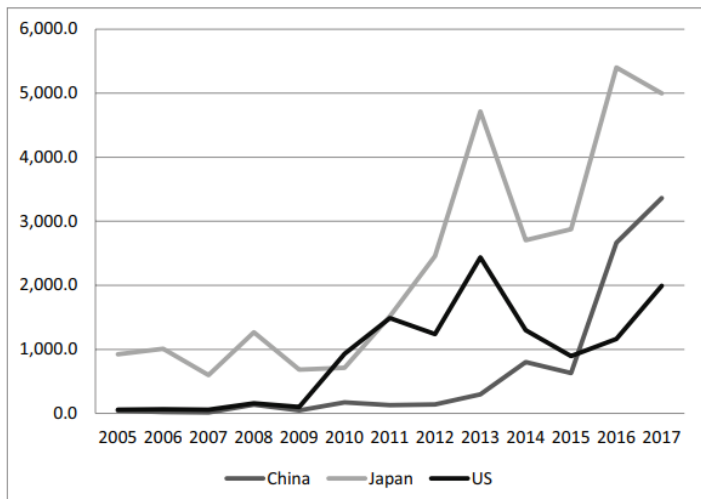


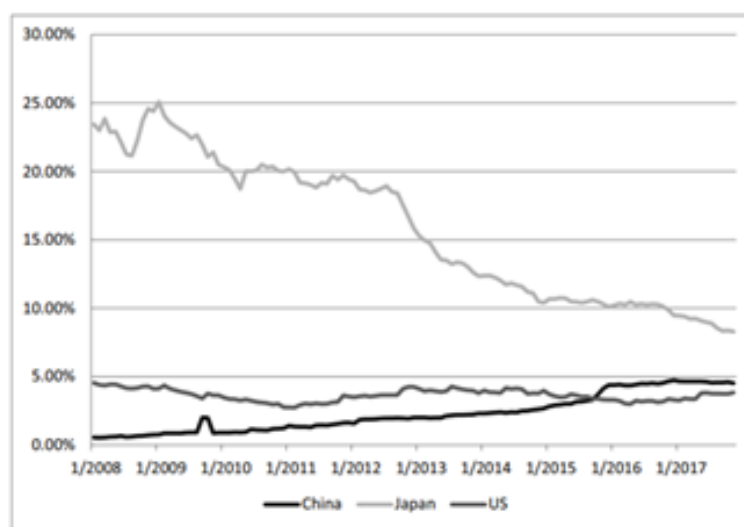
Figure 9 (Textor, 2021)



4.3 External debt

The main characteristic of the debt situation between China and Indonesia is a gradual growth in Indonesia's debt to China since at least 2008. The result is that China has become the second largest loan provider for Indonesia. Chinese loans to Indonesia have expanded from 800 million U.S. dollar to 17.75 billion U.S. dollar in 2019. This is a significant amount as it is 5 percent of Indonesia's total foreign debt and China is Indonesia's second most important loan provider (Negara & Suryadinata, 2019; M. Z. Rakhmat, 2020b). 92 percent of these loans go to the private sector, only a small percentage is from the government. In 2008, the Chinese debts were 0.6 percent of Indonesia's total foreign debt. This rose to 4.5 percent in 2017 (Negara & Suryadinata, 2019).

Figure 10: Indonesia's external debt by three major donors (percentual share of total external debt) (Negara & Suryadinata, 2019, p. 11)



4.4 The hypotheses

In conclusion, China and Indonesia have a growing economic interdependence that gradually started to develop around the turn of the century. However, this relationship has developed extremely unequal and created significant economic dependence from Indonesia on China. Following from this conclusion, we can use the theoretical framework from chapter 2 to come up with the following hypotheses:

Transform mechanism

The transform mechanism would hypothesize that a stronger economic relationship would cause both Indonesia and China to become less interested in owning territory. However, hypothesis 1 only includes China, because in this case Indonesia already owns the Natuna territory. The second hypothesis is that economic exchange will lead to the alignment of their foreign policy goals.

1. *China has become less interested in the Natuna area over time, but increasingly interested in investing in the development of the Natuna area and/or importing goods from the Natuna area.*
2. *China's and Indonesia's foreign policy goals regarding the Natuna area have become more aligned over time.*

Alternative inform mechanism

Given that their economic relationship is asymmetric, this thesis will utilize the alternative inform mechanism instead of the regular one. Moreover, given that China is the dominant party in the relationship it is hypothesized that China will utilize this power to obtain its foreign policy goals through bluffing and economic sanctions. Indonesia would not have the power for these strategies.

3. *China has increasingly used bluffing in the Natuna dispute.*
4. *As a reaction to China's bluffing, Indonesia has increasingly resisted China.*
5. *China has increasingly used (threatening with) economic sanctions in the Natuna conflict.*

Constrain mechanism

Given that Indonesia is economically dependent on China but not the other way around, but also taking into account states are not a unitary actor. The constrain mechanism comes up with the following hypotheses:

6. *Indonesian domestic actors who profit from the economic relationship with China have become increasingly constrained by the economic relationship with China to let the Natuna conflict escalate.*
7. *Indonesian domestic actors who economically profit from the Natuna area are in favor of policies with the aim to protect the Natuna area*

5. An analysis of the Natuna territorial dispute

This chapter provides an analysis of the Natuna territorial dispute. The first section gives an introduction to the Natuna territorial dispute, including some introductory information about the Natuna Islands themselves, the South China Sea and a small overview of the development of the Natuna territorial dispute. The second part of this thesis lays out the analysis of the dispute. This section discusses the several theoretical mechanisms of this thesis and their hypotheses one by one.

5.1 Introduction to the Natuna territorial dispute

The Natuna archipelago is located in the most northern region of Indonesia (see figure 11). It is actually located between the two main islands of Malaysia, more than a thousand kilometers from Jakarta. The archipelago consists of 262,000 square kilometers of water and 154 islands, of which only 27 are inhabited. The amount of water is more than 10 times the total size of the islands (R. A. Supriyanto, 2015). The Natuna islands have about 81,000 inhabitants (Yulisman, 2020). They claim to have more cultural and historical ties with Malaysia. The area is economically valuable because it has one of the largest untapped gas fields in the world, an estimated 210 trillion cubic feet. Moreover, it is a popular fishing ground (Johnson, 1997, p. 153). The fact that the islands are so spread out and far from the rest of Indonesia make them hard to control and monitor (R. A. Supriyanto, 2015). This makes the area prone to illegal fishing by foreign fishermen from not only China, but also Vietnam, the Philippines and Malaysia (Chan, 2017).

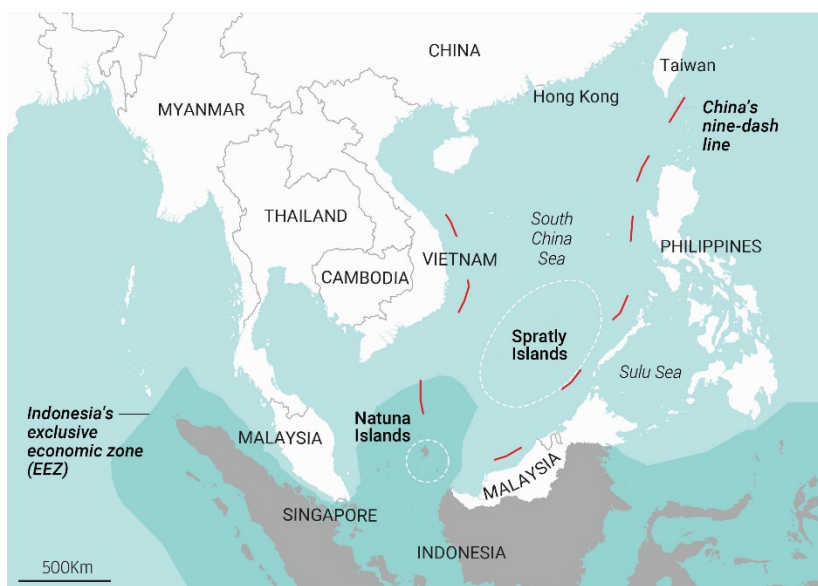
The borders of the Natuna Islands have been listed according to the United Nations Convention on the Law of the Sea (UNCLOS) (Prameswari, 2020). This treaty from 1982 establishes that the Natuna archipelago is part of Indonesia's Exclusive Economic Zone (EEZ). This means that Indonesia has "sovereign rights for the purpose of exploring and exploiting, conserving and managing the natural resources" (United Nations Convention on the Law of the Sea, p. 43). UNCLOS has been signed by both Indonesia and China. Indonesia ratified the treaty in 1985 and China in 1996 (Darusman et al., 2020).

The dispute about the Natuna area started in 1993, during a workshop that Indonesia had organized about managing potential conflicts surrounding the South Chinese Sea. During this workshop, China presented a map in which it laid out their "historic claims." These claims included almost the entire South China Sea, including a part of Indonesia's EEZ, close to the Natuna Islands. However, at the time Indonesia decided to ignore the issue as China's claims were ambiguous as they had not even included specific coordinates. The issue only reached the public in 1995. However, after one military exercise on the Natuna Islands in 1996, the situation cooled down to only surface again more than ten years later (Johnson, 1997). In 2009, China officially submitted the (still ambiguous) map with the nine dash line to the UN (Roy, 2016, p. 224). Since then, China has increased its naval activities close to the border of Indonesia's EEZ. Moreover, there has been increased illegal fishing in Indonesia's EEZ (Parameswaran, 2016). The Natuna conflict is mainly characterized by confrontations between illegal Chinese fisherman and the Indonesian coast guard in Indonesia's EEZ. At first, Indonesia tried to play down the issue. This changed in 2014, when Indonesia installed a new government. The new president, Joko Widodo, made clear that he intends Indonesia to become a maritime power and that it will take more action to combat illegal fishing (Parameswaran, 2015a). The issue of illegal fishing was taken up by the new minister of fisheries, Susi Pudjiastuti. She announced the policy to blow up vessels that intruded the Indonesian EEZ (Beech & Suhartono, 2018). Once this policy was implemented, the amount of illegal Chinese vessels reduced significantly (Beech & Suhartono, 2020). However, tensions rose in 2016, when there were three high-profile confrontations between Chinese fisherman and the Indonesian coast guard (Panda, 2016). The "blow up vessels" policy ended in 2019 and resulted in the immediate return of illegal fisherman in the area. At the end of 2019, there was another large

escalation. There was a stand-off between Chinese boats and Indonesian warships for months (Sulaiman, 2020). In 2021, China has told the Indonesian government to stop drilling in China's territory. Indonesia firmly rejected their request (Allard et al., 2021). As a response to these hostilities in the past years, Indonesia has increased military power and organized several military exercises in the Natuna region (M. Z. Rakhmat, 2020a).

The Natuna islands dispute is not the only dispute in the area. The South China Sea² has been a hotspot for territorial disputes for more than decades (Raine & Le Mière, 2017, pp. 29–30). The sea does not only carry a third of all maritime traffic, but also rich of resources. It has an estimated 11 billion barrels of untapped oil and 190 trillion cubic feet of natural gas. There are several countries involved in disputes, for instance China, Indonesia, Malaysia, the Philippines, and Vietnam (Center for Preventive Action, 2022). One of the main issues is the ownership of the Spratly Islands and China's Nine Dash Line which covers almost the entire area (see figure 11). This line has been critiqued for being unclear and having no basis in modern international law (Roy, 2016, p. 224). In 2013, the Philippines even sued China over the issue. In 2016, the Permanent Court of Arbitration in The Hague ruled that the nine-dash line was legally baseless. However, China ignored this ruling (Rosenfeld, 2016)

Figure 11: a map of Indonesia's EEZ and China's nine-dash line (Siow, 2021)



5.2 empirical analysis

5.2.1 Transform mechanism

The transform mechanism had two related hypotheses:

1. *China has become less interested in the Natuna area over time, but increasingly interested in investing in the development of the Natuna area and/or importing goods from the Natuna area.*

² This is the most common name for the sea. However, even the name of the sea is highly disputed (Roy, 2016).

- 2. China's and Indonesia's foreign policy goals regarding the Natuna area have become more aligned over time.*

Both hypotheses are rejected as the increased economic exchange between China and Indonesia has not transformed their political interests. On the contrary, China has become more and more explicit in its interest in owning the Natuna area, more specifically the Natuna gas fields. At first it was always vague about which territory it was claiming exactly with the nine-dash line map, even when it officially submitted the map to the UN in 2009 (Roy, 2016, p. 224). In 2016, during the three high-profile confrontations that year, it was the first time that China stated for the first time that the nine-dash line included "traditional fishing grounds" within Indonesia's EEZ (AP Editors, 2016). Not only has it been more explicit in its interest in owning the Natuna area, it has also been increasing military activity in the area since 2009 (Beech & Suhartono, 2020). Indonesia has also become more explicit over the years in its commitment of maintaining its sovereignty over the Natuna islands, especially since 2015 when tensions started to rise. In 2016, as a response to the rising tensions, the president even held a cabinet meeting aboard a warship off the Natuna islands (Kapoor & Jensen, 2016). He has also made statements about protecting Indonesia's territory that have been characterized as unusually strong by the press. In 2016, in the State of the Union address, the president pledged to defend "every inch" of Indonesia's land and maritime territory (The Straits Times, 2016b). In 2019, during a visit to the Natuna islands as a response to the incident with China, the president said "There is no compromise on our sovereignty." Moreover, the government has also started to militarize the area and has organized more and more military exercises in the area since 2015 (The Straits Times, 2016a)

It has also never been reported that China has even showed interest in investing in the Natuna region or in importing its resources. In contrast, Indonesia has often encouraged foreign countries and businesses to invest in the development of the Natuna project. The first time was in 1997, at the start of the conflict (Richardson, 1997). In 2020, the Indonesian government also asked Japan and the United States to consider investing in the Natuna islands (Rekhi, 2020; The Straits Times, 2020). At this point in time, the dispute has been going on for so long that Indonesia would probably be suspicious if China would want to invest in the Natuna islands. However, Indonesia's behavior shows that it is not inherently opposed to FDI in the Natuna region.

In conclusion, the growing economic relationship between Indonesia and China has not resulted in them becoming less interested in territory as a way to obtain resources. Regarding the Natuna dispute, their foreign policy interests have only become more explicitly opposing.

5.2.2 Alternative inform mechanism

Now that we know increased economic interdependence has not affected the interests of Indonesia and China, the following mechanisms assessed whether it would affect their behavior. The alternative inform mechanism had the following corresponding hypotheses:

- 3. China has increasingly used bluffing in the Natuna dispute.*
- 4. As a reaction to China's bluffing, Indonesia has increasingly resisted China.*
- 5. China has increasingly used (threatening with) economic sanctions in the Natuna conflict.*

The first two hypotheses are accepted as the growing asymmetrical economic relationship between Indonesia and China has resulted in gradually more bluffing by China and resistance to this bluffing by Indonesia. This gradual change has become visible since the 2010s, when Indonesia's economic dependency on China had started to become significant. Since this period, the conflict can be characterized by a continuing but gradual increase from bluffing and pressure by China and a careful but growing resistance by Indonesia. However, the last hypothesis is rejected because explicitly using economic power as a tool has not occurred in the Natuna dispute.

In the 1990s and early 2000s, the economic relationship between Indonesia and China was still weak. In this period, China did start the dispute, but besides that it did not undertake much at all regarding the dispute. All the incidents that occurred were an response from Indonesia to China starting the conflict. When China first presented the nine-dash line during the Spratly workshop in 1993, Indonesia's only response was to send a diplomatic note (Johnson, 1997, p. 154). This note only became public in 1995, Indonesia's Foreign Minister asked China for clarification regarding their claim of the area close to the Natuna Islands (Johnson, 1997, p. 155). However, China did not offer clarification. As a response, Indonesia held a small naval exercise in the Natuna area and officially stated that they were prepare to defend the Natuna territory. As a response, China verified that there was no territorial dispute over the Natuna islands, but that they were willing to discuss their sea borders with China. Indonesia's response was that there was no need to discuss sea borders (Johnson, 1997, p. 157). The next years, they organized two military exercises. Besides this, the issue died down because China did not make any moves (Johnson, 1997, p. 159). As Indonesia's behavior was reactionary, it also did not do anything. The only bluffing from China's side in this period was the initial presentation of the nine-dash line. However, they never followed up their words with actions (Johnson, 1997). Besides this incident there was no bluffing or other action from China for many years.

The next time China bluffed is when it officially submitted the map with the nine dash line to the UN in 2009. Despite several calls from experts and foreign governments for clarification, China has kept their claims ambiguous. They do not clarify which area they specifically claim and what type of ownership they want (Roy, 2016, p. 224). Moreover, it has not backed up their claim with action as they did not clarify their claim or annex the Natuna region. Instead, China slowly started to put pressure on Indonesia by increasing illegal fishing in their EEZ (Parameswaran, 2016).

This move by China has been met with increased resistance from Indonesia. At first, they tried to downplay the incidents with Chinese fisher boats and kept them out of the media (Parameswaran, 2016). The first incident that was met with harder resistance from Indonesia occurred in 2013. In that year, a Chinese fisher boat was arrested for illegal fishing. However, the Indonesian coast guard was forced by a maritime law enforcement vessel from China (Cochrane, 2016). This time, the incident was not kept under wraps. It received wide media attention and the Indonesian government summoned the Chinese ambassador. Although China responded that the Chinese fishermen were fishing in traditional Chinese fishing grounds, they did not take any further action (Cochrane, 2016).

However, in march 2014 China continued to bluff when it started to include the Natuna waters on the new maps on Chinese passports (Keck, 2014). This was met by more resistance by Indonesia. In 2014, a new cabinet introduced the "sink the vessel" policy. This was mainly framed as an economic issue rather than one of sovereignty. The Indonesians stated they were mainly worried about annual losses of over \$20 billion cause by illegal fishing (Parameswaran, 2015a; Swaragita, 2019). However, an interview with the Fisheries minister at that time in the New York Times shows it was indeed a subtle move against the Chinese. The interview reports: "with the other hand, she simulated grinding a stiletto heel into the ground. "This is what I can do if the Chinese try to play tricks on me," said Ms. Pudjiastuti, the maritime affairs and fisheries minister of Indonesia. "I can smile very nicely and then I

can use my high heel.” Another comment by her was: “I’m not the military, I’m not the foreign minister,” she said. “The Chinese cannot really get angry at me because all I’m talking about is fish” (Beech & Suhartono, 2018).

Despite Indonesia’s resistance, China has always continues to put pressure on Indonesia after a while. In this period Chinese vessels started to enter deeper into the Indonesian EEZ with larger vessels (Panda, 2016). This was met by more resistance from Indonesia, which resulted in three high profile incidents in 2016. In March, the Indonesian authorities arrested another Chinese fisher boat. However, the Chinese Coast Guard rammed the Chinese boat to free it. The Indonesian authorities were furious over the incident and the minister of fisheries called China “arrogant.” They also summoned the Chinese ambassador and sent out an official letter of protest. This was seen as a change of attitude from Indonesia. China simply responded similar as before, by stating the fishermen were fishing in traditional Chinese fishing grounds (Panda, 2016).

In May, the Indonesian Coast guard fired warning shots and arrested another Chinese boat. This time, the Chinese protested, but not reiterate the traditional fishing grounds argument (AP Editors, 2016). At last, in June, a similar incident occurred. After this incident, the Chinese Foreign ministry claimed that Indonesia had abused its military force. Moreover, it stated for the first time that the nine-dash line included “traditional fishing grounds” within Indonesia’s EEZ (The Straits Times, 2017b). As a response, the Indonesian president responded unprecedently strong by hosted a cabinet meeting on a warship in the Natuna region a few days later. China responded that it does not dispute Indonesia’s sovereignty of the Natuna islands, but that there were some overlapping maritime claims. Therefore, they were hoping Indonesia could meet them half-way. However, they did not take any further action (Kapoor & Jensen, 2016).

In the State of the Union address in August 2016, the president pledged to defend "every inch" of Indonesia’s territory. The defense budget for 2016 was also increased by almost 10 percent (Setiaji & Beo Da Costa, 2016). Furthermore, the Indonesian military staged two military exercises in the Natuna area in October 2016 and May 2017 (Soeriaatmadja, 2019; The Straits Times, 2017a). The government also started to look for allies in maritime security, for instance with Australia, Japan, India, US and other South East Asian countries (Chan, 2016, 2018; Ganapathy, 2016; Suryadinata & Izzuddin, 2017; The Straits Times, 2018).

In July 2017, Indonesia renamed the sea around the Natuna Islands as “the North Natuna Sea.” China requested Indonesia to cancel the decision (Parameswaran, 2017). However, this was another bluff from China, because when their request was not met, they did not take any further action. There was a new round of escalations at the end of 2019, when China once again went one step further in provoking Indonesia. On the 19th of December a group of around 60 Chinese fishing vessels and coast guards entered the Indonesia EEZ. This led to a giant stand-off between Chinese boats and Indonesian warships and F-16 fighters. They shadowed each other around the Natuna gas fields (Sulaiman, 2020). As a response, Indonesia protested to Beijing and eventually send the president to visit the Natuna islands. There, he made a unusual strong statement: “There is no compromise on our sovereignty.” The next day, it became clear China was merely bluffing when the Chinese vessels finally decided to leave the EEZ (Yulisman, 2020).

in July 2020, Indonesia held another military exercise in the Natuna area. However, Indonesia has not only resisted with exhibiting military power (Rakhmat, 2020a). In May 2020, Jakarta entered a diplomatic note to the UN in which it rejected China’s claims in the South China Sea on the basis of UNCLOS (Rakhmat, 2020a) .

In 2021, China requested the Indonesian government to stop drilling for gas in the Natuna area because it is China's territory. The Indonesian government firmly rejected their request. However, the Chinese never took any action afterwards (Allard et al., 2021).

This data shows us that bluffing and resisting is happening more subtle than theories propose. Although China has been increasingly persistent in the Natuna dispute, they have also been holding back. If the government wanted to, they could use harsher measures against Indonesia to obtain the Natuna territory. They could for instance use military force, given that Indonesia's military is still limited compared to China despite recent growth (Parameswaran, 2015a). Moreover, they could also threaten with or introduce economic sanctions, given Indonesia's economic dependence on China.

China's way of bluffing has not been to explicitly leverage its economic (or military) power by using costly signaling methods like (threatening with) economic sanctions or military action. Rather, China's method has been more subtle through the use of Chinese fisher boats illegally entering Indonesia's EEZ but most often ending up backing down in the end. Their other method of bluffing has been releasing often ambiguous statements and maps that the Natuna islands are theirs but never taking clarifying their claims or taking action over the issue.

It is likely that the China is not holding back for direct economic reasons. What is more important than the economic ties with Indonesia is China's reputation in South East Asia (SEA). Indonesia is an important and well-respected regional power in SEA, for instance due to its significant role as a mediator in regional conflicts. It is also often considered to be the de facto leader of the ASEAN (Acharya, 2015, pp. 1–2). China's reputation in SEA is important because it is a strategically important and because it is China's geographic backyard (Ferchen, 2022; Shambaugh, 2018). If China would damage its relationship with Indonesia too much, this will hurt its reputation in the region and hurt its geopolitical standing in the world. Moreover, if China would (threaten with) economic sanctions this would probably scare off many economic partners of China. If China would be become known as an unreliable business partner, this would lead to countries trying to reduce their economic ties with China due to the potential risks. This might explain why China has made an explicit statement stating it wants to continue investing in Indonesia (Akhlas, 2020). However, more research would be necessary to verify this hypothesis.

5.2.3 constraint mechanism

The constraint mechanism proposes the following three hypotheses:

6. *Indonesian domestic actors who profit from the economic relationship with China have become increasingly constrained by the economic relationship with China to let the Natuna conflict escalate.*
7. *Indonesian domestic actors who economically profit from the Natuna area are in favor of policies with the aim to protect the Natuna area.*

The constraint hypotheses are all accepted, as actors in the Natuna dispute are indeed influenced by their economic interests that arise from the economic relationship between Indonesia and China. However, it has to be noted that the Natuna territory also has economic value and therefore certain actors are influenced by two opposing interests. The mechanism also hypothesized that China would be less constrained to let the dispute escalate because the economic relationship with Indonesia is not

that important for the Chinese economy. This hypothesis is also accepted. However, it is theorized that China is constrained to let the conflict escalate by non-economic factor, namely international reputation. It might seem contradictory that the countries can both be bluffing/resisting, as explained in the last section, while being constrained at the same time. However, this section shows how both countries balancing several interests at the same time. This section will discuss the following actors one by one: The Indonesian national government, the general public in Indonesia and the fisherman from Natuna who are directly involved in the dispute.

5.2.3.1 The Indonesian national government

The Indonesian national government is the actor that is the most conflicted between two economic interests. On the one hand, the resources of the Natuna islands are economically valuable, especially the gas fields. On the other hand, the government is also profiting from its economic relationship with China. The last section laid out how Indonesia has been increasingly resisting China in the Natuna dispute due to the economic worth of the territory. However, there is also sound evidence that Indonesia has also been constrained in reacting to China. The current government has increased its economic ties with China, for instance by promoting Chinese investment projects like the Jakarta-Bandung high-speed railway (Siow, 2021). Therefore, their strategy has been a balancing act between resisting China but maintaining relatively friendly relations at the same time.

The most important piece of evidence for this is that when Indonesia installed the sink the vessels, they started to blow up foreign vessels right away, but took a more careful approach with China compared to the Philippines, Malaysia and Vietnam. Compared to China, these countries are not significant trade partners of Indonesia (Data from APEC Statistics, Bilateral Linkage Database – Trade Flows) In December 2014, Indonesia captured several illegal Chinese vessels without sinking them. However, the government did cancel a deal with China regarding cooperation in the fisheries sector early 2015 (Parameswaran, 2015b). The first Chinese boat was blown up in May 2015. However, the boat in question had actually been captured in June 2009. In contrast to boats from other countries, it was blown up among a big group of boats of different nationalities. The minister of fisheries also emphasized that it was not a show of force, but that she was merely enforcing Indonesia's laws (Parameswaran, 2015b) not do It seemed like a strategic choice from Jakarta to blow it up at that particular moment. It was also obviously holding back on blowing up Chinese boats (Parameswaran, 2015c). After this incident, Indonesia did not blow up other boats. It was reported in April 2017 that the government has confiscated and destroyed 317 foreign vessels since 2014: 142 from Vietnam, 76 from the Philippines, 49 from Malaysia, but only one from China (Chan, 2017).

In 2019, the fisheries minister of the "sink the vessels" policy, Susi Pudjiastuti, was not rechosen despite the immense popularity of her and her policy. The year before, Indonesia's vice president publicly complained that the policy was scaring of investors (Beech & Suhartono, 2018; Scarpello, 2020, p. 131). Scarpello (2020) has interviewed 30 insiders from the fisheries industry and discovered that both the vice president, Jusuf Kalla, and a minister, Luhut Padjaitan, were heavily lobbied by that sector. One of their aims was to get Pudjiastuti removed from office or at least let her end the sink the vessels policy. The fisheries sector in Indonesia is rampant of breaching regulations and links with foreign companies or investors. There were many foreign investors who indirectly owned fisheries companies, for instance from China. Therefore, the sink the vessels policy was not in their interest. Moreover, Luhut Padjaitan was also consistently lobbied by Chinese business interests. Both senior politicians have asked Pudjiastuti to cancel her policy. Allegedly, they also advised the president to remove her from office.

Public statements that politicians make about the Natuna dispute also suggest they are constrained by Indonesia's dependency on China. The government is notorious for downplaying incidents to appease China (R. Supriyanto, 2016). During the incident at the end of 2019, the Indonesian president first visited the Natuna islands and stated that "There is no compromise on our sovereignty." However, later he downplayed the incident when he wrote on Facebook: "I asked the Indonesian military Commander, are there foreign ships entering Indonesian territorial sea? As it turns out, none" (Arshad, 2020).

5.2.3.2 The general public in Indonesia

As both the Natuna islands and economic ties with China are generally profitable for Indonesia, the constraint mechanism would hypothesize that the general public would be conflicted just like the government. However, the public opinion in Indonesia is in favor of harsh policies against China, for instance minister Pudjiastuti and her sink the vessels policy were incredibly popular. She was considered to be a political superstar at the time (Beech & Suhartono, 2018; Scarpello, 2020). The reason for this is that the majority of Indonesians do not feel like they are profiting from the economic ties with China. Rather, the view is that only the Chinese minority in Indonesia is profiting. Gammeltoft & Tarmidi (2013) have noted that due to shared language and cultural ties, Chinese investors are more likely to partner with Chinese Indonesian businesses than those of indigenous Indonesians. This also has to do with the dominant role Chinese Indonesians play in the private sector (Gammeltoft & Tarmidi, 2013, p. 140). Moreover, Chinese companies in Indonesia have led to the influx of at least 25,000 foreign Chinese workers, because these companies prefer to work with Mandarin speakers. This has resulted in resentment among indigenous Indonesians (Koesoemawiria, 2021a).

5.2.3.3 Local fishermen from the Natuna region

There are several actors that are directly involved in the fisheries sector of the Natuna area. However, due to the limited scope of this study, these actors will only be discussed briefly. One of the actors involved are the local fishermen from the Natuna islands. They have often urged the government to implement stricter policies against illegal (Chinese) fishing in the area. They accuse illegal fishermen from stealing their fish and overfishing in the area (Beech & Suhartono, 2018; Yulisman, 2021). Moreover, in 2019, there has also been an incident in which an Indonesian fisherman was repelled by the Chinese coast guard in the Indonesian EEZ (Ng, 2020). Their case proves that domestic actors who directly benefit from the Natuna area and not from economic exchange with China are not constrained by China but are in favor of policies that protect the area.

6. Conclusion

The aim of this thesis is to answer the following research question:

“How has the development of the economic interdependence between China and Indonesia affected their behavior in the Natuna territorial dispute?”

China and Indonesia have developed their economic relationship since the turn of the century. However, this has been asymmetrical so it has created Indonesia to become economically dependent on China. This growing dependence has not transformed the interests of both countries but it has influenced their behavior in other ways. China has increasingly used bluffing in the Natuna dispute and as a reaction Indonesia has increasingly resisted China. This has led to more incidents and incidents with a higher level of hostility over time. However, economic sanctions have not been used as a bluffing technique. This could be because it would hurt China’s reputation in SEA and its reputation as a reliable business partner. Therefore, it could hurt China geopolitically and economically in the long run, even if the direct economic effects are not large. However, further research would be necessary to confirm this. Increased economic exchange has on the one hand led to Indonesia to resist China harder. However, it has also constrained Indonesia in its actions. This seems to be a balancing act between the economic interests of the Natuna territory and its relationship with China. However, Indonesia is not a unitary actors and different domestic actors have different interests.

The fact that Indonesia still feels constrained by its dependence on China, while China has even reassures Indonesia it wants to continue investing shows that China is still profiting from its economic power without leveraging it explicitly. China’s subtle strategy is successful. It is leveraging its economic power without extremely damaging its relationship with Indonesia.

The most important theoretical take-aways from this thesis are the following: Firstly, the asymmetry of economic relations are vital for understanding their effect on conflict. Secondly, it is also crucial to distinguish between different domestic actors when analyzing conflicts.

The limitations of this thesis are manifold. The most important limitation is that this case study is not possible to provide solid proof for a causal relation. The only way to have solid proof for a causal relation in this case is if the actors admitted that economic interdependence had influenced their decisions. Apart from some statements by Indonesian politicians, this is not the case. It would have been better to not only use the Natuna case, but to investigate more cases. This could have been done by analyzing more territorial disputes with similar circumstances or by analyzing other indicators of the relationship between Indonesia and China. However, the scope of this thesis was too limited to do this. The second limitation of this thesis is that the publicly accessible data about the economic relation between China and Indonesia is rather limited. This section of this thesis would have been stronger if there had been more specific data available.

There are several recommendations for future research on this topic. First of all, like already mentioned in the limitations section, it would be interesting to analyze more territorial disputes with similar circumstances or by analyzing other indicators of the relationship between Indonesia and China. Another interesting direction would be to further investigate the effect economic interdependence can have on different domestic actors. This thesis slightly touches upon this topic, but it has not been the main focus on this thesis. At last, the majority of research in this field has been quantitative. However, I would like to argue that due to uncertainty regarding causal mechanisms it would be more useful to perform qualitative research with a small sample size.

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