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## INDONESIA'S ECONOMIC DIPLOMACY STRATEGY IN NAVIGATING US-CHINA COMPETITION IN THE INDO-PACIFIC REGION: RECOMMENDATIONS FOR POLICY MAKERS

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### ABSTRAK

Dinamika konflik kepentingan AS-Tiongkok di Indo-Pasifik menciptakan tantangan dan peluang ekonomi bagi Indonesia. Penelitian ini mengkaji strategi **diplomasi ekonomi** Indonesia sebagai **hedging** untuk menavigasi persaingan ini dan memaksimalkan kepentingan nasional (2014-2024). Menggunakan studi kasus kualitatif, temuan menunjukkan Indonesia menerapkan *hedging* kompleks. Strateginya menggabungkan **soft balancing** terhadap kedua negara (misalnya, melalui kerja sama Quad) dengan **economic bandwagoning** (menarik investasi dan berpartisipasi dalam BRI). Pendekatan ganda ini memungkinkan Indonesia mempertahankan **otonomi strategis** dan memanfaatkan keuntungan ekonomi. Diplomasi ini dinilai berhasil mengurangi risiko dan memanfaatkan peluang, walau menghadapi tantangan keberlanjutan. Studi ini berkontribusi pada praktik non-blok modern dan fleksibilitas strategis regional.

**Kata Kunci:** Diplomasi ekonomi, strategi hedging, kompetisi AS-Tiongkok, Indo-Pasifik, Indonesia.

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### ABSTRACT

The dynamic US-China conflict of interest in the Indo-Pacific creates economic challenges and opportunities for Indonesia. This study examines Indonesia's **economic diplomacy** strategy as **hedging** to navigate this rivalry and maximize national interests (2014-2024). Using a qualitative case study, findings show Indonesia implements complex *hedging*. The strategy combines **soft balancing** against both powers (e.g., through Quad cooperation) with **economic bandwagoning** (attracting investment and participating in the BRI). This dual approach enables Indonesia to maintain **strategic autonomy** and leverage economic gains. The diplomacy is deemed successful in mitigating risks and exploiting opportunities, despite sustainability challenges. The study contributes to modern non-alignment practices and regional strategic flexibility.

**Keywords:** Economic diplomacy, hedging strategy, US-China competition, Indo-Pacific, Indonesia

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## BACKGROUND

Over the past ten years, the structure of global geopolitics has undergone a significant reorientation toward the Indo-Pacific region. This transformation reflects not merely a geographical reorientation but a comprehensive restructuring of power dynamics encompassing military, economic, and technological dimensions. As the two biggest economies globally, the United States and China have progressively treated the Indo-Pacific as the central arena of their strategic rivalry extending beyond traditional military posturing to include trade wars, technological competition in 5G and 6G networks, artificial intelligence development, and control over global supply chains (Goldstein 2020).

The escalating strategic competition between the United States and China has emerged as a central element of modern international affairs, especially within the Indo-Pacific landscape. Over the past decade, China's rapid military modernization, expanding economic influence through the Belt and Road Initiative (BRI) along with Beijing's growing assertiveness in the South China Sea have challenged the long-standing U.S.-led regional order (Mearsheimer 2019). As a countermeasure, the United States has strengthened its regional alliances, advanced the vision of a Free and Open Indo-Pacific (FOIP) accompanied by the United States deepening strategic outreach to the Southeast Asian region (Campbell and Ratner 2018). The intensifying competition spans the areas of security, trade, technology, and political influence, offering both opportunities and challenges for the region's middle powers, including Indonesia.

For Indonesia, the nation with the fourth highest population globally and the southeast Asia region's largest economic power, the U.S. and China rivalry carries profound implications. Geographically positioned at the Indo-Pacific's key maritime intersection diplomatically committed to ASEAN centrality, Indonesia must navigate between major powers while safeguarding its sovereignty and economic interests. The country relies heavily on China for trade and investment, particularly in infrastructure and industrial development, yet simultaneously maintains strong security and diplomatic relations with the United States (Laksmana 2019). Moreover, the intensifying competition in the South China Sea directly influences Indonesia's strategic sphere, particularly in the North Natuna Sea region.

Given these dynamics, Indonesia increasingly employs a hedging strategy—a foreign policy approach that avoids choosing sides between competing major powers while simultaneously engaging and balancing them to reduce risks (Kuik 2008). Economic diplomacy serves as the primary instrument through which this hedging strategy operates. Economic diplomacy, defined here as the use of trade, investment, and financial instruments to achieve national strategic goals, enables Indonesia to simultaneously engage both powers economically while maintaining political equidistance. Rather than security alliances or ideological alignment, economic diplomacy allows Indonesia to attract capital for infrastructure development, secure

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technology transfers for industrial upgrading, diversify investment sources to avoid dependency, and leverage competing offers to maximize benefits—all while preserving the strategic autonomy central to Indonesia's non-aligned foreign policy tradition.

This instrumental relationship between economic diplomacy and hedging strategy manifests concretely: Indonesia participates under China's broader Belt and Road Initiative framework to secure infrastructure financing while simultaneously engaging in US-led initiatives like the Indo-Pacific Economic Framework; accepts Chinese investment in downstream industries while negotiating technology partnerships with Japan and South Korea; and maintains defense cooperation with the United States while expanding maritime security collaboration with India and Australia. Economic diplomacy thus functions as the operational mechanism that transforms hedging from an abstract strategic concept into concrete policy actions (Kuik 2016).

The Jokowi administration (2014-2024) particularly emphasized infrastructure development, industrial upgrading, and foreign investment attraction as key pillars of national development strategy, mobilizing over \$412 billion in infrastructure investment during this period, with foreign sources contributing approximately 35% (Bappenas 2024).

This study addresses a central question: How does Indonesia leverage its economic diplomacy to navigate US-China competition without aligning with either bloc while maximizing national benefits, and to what extent does Indonesia's diplomatic positioning influence the strategic calculations of both competing powers? This question encompasses several subsidiary issues including the specific mechanisms through which Indonesia engages both powers, the theoretical frameworks that best explain these practices, the effectiveness of these strategies in achieving stated national objectives, and the degree to which Indonesian agency shapes regional dynamics rather than merely responding to external pressures.

This research makes several contributions to existing scholarship. It explains Indonesia's practice of non-alignment in the modern era within an economic context, moving beyond traditional security-focused analyses. The study provides an analytical framework for understanding Indonesia's strategy in the Asia-Pacific region that can be applied to other middle powers facing similar dilemmas. Additionally, it offers policy recommendations grounded in theoretical analysis and empirical evidence that can inform future diplomatic practice.

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## LITERATURE REVIEW

### Hedging Strategy

Hedging represents one among the leading significant theoretical developments within the field of international relations studies over the past two decades, offering analytical purchase on state behavior that defies conventional realist dichotomies. The concept emerged from sustained observation that numerous states, particularly in Asia, refused to align exclusively with either the United States or China despite intensifying strategic competition between these powers.

Kuik's (2008) seminal work establishes hedging as a distinct strategic posture characterized by deliberate ambiguity and portfolio diversification in international alignment. He characterizes hedging as a strategic approach used to avoid, or anticipate, circumstances where states cannot commit to more definitive choices such as balancing, aligning with a major power, or adopting neutrality. This formulation recognizes that uncertainty about future power configurations and alliance reliability creates incentives for states to pursue multiple, sometimes contradictory, policy options simultaneously.

The multidimensionality of hedging proves central to its analytical utility. Kuik (2016) identifies six constituent dimensions that states may employ in various combinations: indirect balancing through limited security cooperation with multiple partners; dominance denial through diplomatic resistance to hegemonic initiatives; economic pragmatism involving commercial engagement regardless of strategic concerns; binding engagement through institutional constraints on major power behavior; limited bandwagoning by accepting certain benefits from a stronger power; and economic diversification to reduce dependence vulnerabilities.

Goh (2005) contributes the concept of 'omni-enmeshment,' arguing that countries in Southeast Asia actively work to weave all major powers into shared regional mechanisms simultaneously, thereby creating multiple relationships that constrain unilateral behavior and provide weaker states with diplomatic leverage. Medeiros (2005-06) emphasizes the temporal aspect of hedging, noting that states hedge precisely because they cannot predict which power will ultimately dominate.

The distinction between soft balancing and economic bandwagoning represents a crucial analytical hinge within hedging theory. Pape (2005) theorizes soft balancing as coordinated diplomatic action, limited security cooperation, and institutional constraints designed to complicate a dominant power's strategic calculations without engaging in direct military competition. Economic bandwagoning involves selective engagement to capture economic benefits while maintaining political independence in other domains (Womack 2016).

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## Economic Diplomacy

Economic diplomacy scholarship provides the second theoretical pillar for analyzing state strategies in great power competition. Baldwin's (1985) foundational work establishes economic statecraft as a distinct category of foreign policy instruments, encompassing trade policy, foreign aid, economic sanctions, investment regulation, and currency manipulation. His analytical framework distinguishes between positive economic statecraft (providing economic benefits to influence behavior) and negative economic statecraft (imposing costs or withholding benefits).

Hirschman's (1945) classic analysis shows that asymmetric economic ties generate structural leverage for the party with lower dependence, as the actor bearing greater dependence incurs substantial costs if the relationship is disrupted. The contemporary resurgence of geoeconomics reflects recognition that economic interdependence can be weaponized for strategic purposes. Blackwill and Harris (2016) argue that major powers increasingly employ economic coercion, investment screening, technology restrictions, and infrastructure financing as instruments of strategic competition. Farrell and Newman's (2019) concept of "weaponized interdependence" illuminates how states controlling critical network nodes can exploit these positions for coercive leverage.

Okano-Heijmans (2011) develops a comprehensive framework for economic diplomacy that distinguishes it from both commercial diplomacy (purely economic objectives) and geoeconomics (overtly coercive economic statecraft). Economic diplomacy refers to the employment of economic instruments to advance foreign policy goals, and the deployment of political resources to support economic aims. This bidirectional relationship recognizes that economic and political objectives intertwine in complex ways.

The concept of economic statecraft has expanded beyond traditional trade and aid to encompass diverse instruments relevant to contemporary competition. Investment diplomacy involves using inward and outward foreign direct investment flows as strategic tools (Jensen et al. 2019). Infrastructure diplomacy, prominently manifested in China's Belt and Road Initiative, employs connectivity projects to build political influence alongside commercial returns (Hillman 2020). Digital diplomacy increasingly involves competition over technology standards, digital infrastructure, data governance, and artificial intelligence development (Goddard 2018).

## Indo-Pacific Conceptualizations and Regional Order

The Indo-Pacific has emerged as the predominant geographic and strategic frame for analyzing Asian regional dynamics, yet the concept itself remains contested and reflects competing visions of regional order. The United States articulated its Free and Open Indo-Pacific strategy emphasizing sovereignty, freedom of navigation, free trade, and rules-based order (US Department of State 2019). The Biden administration

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refined this approach through the Indo-Pacific Strategy released in 2022, maintaining core principles while emphasizing multilateral coordination and economic engagement through the Indo-Pacific Economic Framework.

Japan contributed significantly through Prime Minister Abe Shinzo's vision of the "Confluence of the Two Seas," articulated in 2007, emphasizing quality infrastructure, capacity building, rule of law, and connectivity (Abe 2007; Nilsson-Wright 2021). Australia's 2017 Foreign Policy White Paper established the Indo-Pacific as Australia's primary strategic focus, identifying the region as increasingly contested and requiring active engagement. India's Act East policy and Indo-Pacific vision emphasize Indian agency and regional connectivity. Modi's (2018) Shangri-La Dialogue speech articulated an inclusive Indo-Pacific concept open to all nations respecting sovereignty and territorial integrity.

ASEAN's response came through the ASEAN Outlook on the Indo-Pacific (AOIP), adopted in 2019, representing ASEAN's effort to maintain centrality and agency amid competing great power initiatives (ASEAN 2019). The AOIP emphasizes dialogue and cooperation over geopolitical competition, promotes ASEAN-centered architecture, identifies four priority areas for cooperation, and insists on inclusive engagement with all regional partners. Indonesia played a leading role in crafting the AOIP, reflecting its historical commitment to non-alignment and institutional diplomacy (Ministry of Foreign Affairs of Indonesia 2019; Connelly 2019).

Acharya's (2014) work on ASEAN's normative power argues that Southeast Asian regionalism has successfully promoted norms of sovereignty, non-interference, and consultative decision-making that shape major power behavior in the region. Ba's (2021) analysis demonstrates how ASEAN has evolved to maintain relevance amid changing power dynamics through institutional proliferation including ASEAN+3, the East Asia Summit, and ASEAN Regional Forum.

### Conceptual Framework

Based on the literature reviewed, this study proposes an integrated conceptual framework that synthesizes hedging theory and economic diplomacy to explain Indonesia's strategic behavior. The framework consists of three interconnected analytical layers:

First, the structural layer identifies the external pressures and opportunities created by US-China competition, including: (a) geopolitical pressures demanding alignment choices; (b) economic opportunities from competing investment and trade offers; (c) technological competition creating choices between digital ecosystems; and (d) institutional contestation between rival regional architectures.

Second, the strategic layer examines Indonesia's hedging response through economic diplomacy instruments, operating along two simultaneous tracks: (a) Soft

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balancing track: diversifying security partnerships beyond traditional alignments, strengthening economic ties with alternative partners (Japan, India, Australia, EU), participating in multiple institutional frameworks, and building technological alternatives to reduce single-source dependencies; (b) Economic bandwagoning track: accepting large-scale Chinese infrastructure investment, participating selectively in BRI projects, leveraging US technology and innovation partnerships, and maximizing bilateral economic benefits from both powers.

Third, the outcome layer assesses the effectiveness of this strategy across multiple dimensions: (a) economic outcomes (investment attraction, growth performance, infrastructure development); (b) strategic outcomes (autonomy preservation, dependency management, regional influence); and (c) sustainability challenges (escalating pressures to choose sides, debt and dependency risks, domestic capacity constraints, potential for great power conflict).

This framework posits that economic diplomacy functions as the operational mechanism linking Indonesia's hedging strategy to concrete policy outcomes, enabling simultaneous engagement with competing powers while maintaining strategic autonomy—a balancing act that becomes increasingly difficult as competition intensifies but remains viable as long as both powers value Indonesian cooperation more than they demand exclusive alignment.

## **RESEARCH METHOD**

This study employs a qualitative research design using a case study approach to examine Indonesia's economic diplomacy strategy during the period of intensifying US-China competition in the 2014-2024 period. The case study method proves particularly appropriate for investigating contemporary phenomena within real-world contexts, especially when boundaries between phenomenon and context are not clearly evident (Yin 2018). This approach allows for in-depth examination of Indonesia's diplomatic behavior, capturing complexity and nuance that quantitative methods might overlook.

The research adopts a descriptive-analytical approach, first establishing what Indonesia has done through detailed description of policies and actions, then analyzing why these patterns emerged and what they reveal about strategic choices and constraints. This research relies on multiple data sources to construct a comprehensive picture of Indonesia's economic diplomacy, including Policy documents such as Indonesia's RPJMN 2020-2024, the Indonesia Maju vision and sectoral policies from key economic ministries, Official speeches by President Jokowi and senior ministers revealing Indonesia's diplomatic positioning Economic data from BKPM, BPS, and infrastructure project records tracking investment flows and trade

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The primary analytical technique employed is qualitative content analysis of documents and speeches, proceeding through familiarization with materials, development of coding frameworks, systematic coding of content, identification of patterns, and interpretation of findings in light of conceptual frameworks. The hedging framework guides analysis by directing attention to indicators of soft balancing (security cooperation with multiple partners, participation in minilateral groupings, statements emphasizing multilateralism) and economic bandwagoning (participation in major power economic initiatives, acceptance of large-scale investments, supportive rhetoric).

The research also employs process tracing to understand causal mechanisms linking external pressures and opportunities to specific policy choices, constructing detailed narratives of key decisions and examining how policies evolved in response to changing circumstances.

## **DISCUSSION**

### **1. The Dynamics of Strategic Rivalry Between the United States and China and Indonesia's Strategic Position in the Jokowi Era**

The escalating strategic rivalry involving the United States and China throughout Jokowi's presidency manifested through multiple measurable dimensions that fundamentally reshaped Indonesia's external environment. Militarily, China's defense expenditure increased from \$216 billion in 2014 to \$292 billion by 2023, as it concurrently broadened its footprint across the South China Sea area by building seven reclaimed islands equipped with defense installations, airstrips, and anti-access/area-denial (A2AD) systems (SIPRI 2024; AMTI 2024). Washington reacted by increasing FONOPs, or naval missions asserting navigational rights, from 4 in 2014 to

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14 in 2023, while reinforcing the Quad partnership and launching AUKUS in 2021 (US Pacific Fleet 2024).

Economically, the competition escalated dramatically: the 2018-2020 US-China trade war imposed tariffs affecting over \$550 billion in bilateral trade, while US technology restrictions expanded from Huawei's 5G equipment to encompass advanced semiconductors, AI systems, and quantum computing, affecting markets worth over \$200 billion (Peterson Institute 2024). China simultaneously accelerated BRI expansion, with cumulative global investments reaching \$1.3 trillion across 152 countries by 2024, while establishing the AIIB (Asian Infrastructure Investment Bank), holding a capital base amounting to \$100 bn as well as 109 member countries (World Bank 2024; AIIB 2024). Washington countered through the Indo-Pacific Economic Framework (IPEF) launched in 2022, encompassing 14 countries representing 40% of global GDP, though offering limited market access compared to traditional free trade agreements (USTR 2024).

Technologically, competition intensified across critical domains: 5G network deployment, where Huawei captured 30% of global market share by 2023 despite US restrictions; semiconductor manufacturing, where China invested \$150 billion in self-sufficiency programs while the US allocated \$52 billion through the CHIPS Act; and artificial intelligence, where Chinese AI companies received \$17 billion in funding in 2023 compared to \$47 billion for US firms (Bloomberg Intelligence 2024; McKinsey 2024).

Within this intensifying competition, Indonesia's position as the leading economy in Southeast Asia—whose GDP reached \$1.32 trillion in 2023, accounting for 36% of ASEAN's total economic output—provided it with strategic leverage in the Indo-Pacific (World Bank 2024). However, this leverage operated primarily through economic diplomacy rather than military balancing. Indonesia's defense spending remained modest at \$24.1 billion in 2023 (representing just 0.8% of GDP), limiting traditional security balancing options (SIPRI 2024). Consequently, the Jokowi administration strategically prioritized economic instruments to navigate great power competition.

This diplomatic approach aimed to: attract capital for national strategic projects, with infrastructure investment totaling \$412 billion during 2014-2024, of which \$144 billion derived from foreign sources (Bappenas 2024); diversify investment sources to avoid structural dependence, achieving a foreign investment portfolio spanning China (18.5%), Singapore (17.3%), Japan (9.2%), United States (7.4%), South Korea (6.8%), and other partners by 2023 (BKPM 2024); negotiate technology transfers essential for downstream industrialization, particularly in nickel processing, electric vehicle batteries, and renewable energy; and leverage Indonesia's market size (275 million people), natural resource wealth (controlling 24% of global nickel reserves), and strategic location to maximize bargaining power with competing powers (USGS 2024).

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Indonesia's engagement with China illustrates the assertive deployment of economic diplomacy. Jakarta welcomed large-scale Chinese financing for BRI-related infrastructure, with cumulative Chinese investment reaching \$47.3 billion during 2014-2023 across sectors including transportation (\$18.2 billion), energy (\$14.7 billion), manufacturing (\$8.9 billion), and telecommunications (\$5.5 billion) (BKPM 2024). Major projects included the Jakarta-Bandung High-Speed Railway (\$7.3 billion), the Java 7 coal-fired power plant (\$4.5 billion), Morowali Industrial Park for nickel processing (\$5.8 billion), and Jakarta MRT Phase 1 (\$1.2 billion) (Ministry of Transportation 2024).

However, Indonesia simultaneously renegotiated terms when financial risks arose, demonstrating sophisticated economic statecraft. When the Jakarta-Bandung HSR experienced cost overruns increasing total project costs from \$5.5 billion to \$7.3 billion, Indonesia refused to deploy state budget (APBN) funds and instead renegotiated loan terms with China Development Bank, extending maturity from 40 to 50 years while reducing interest rates from 2% to 1.75% (Ministry of Finance 2023). Similarly, when Chinese nickel processing companies were linked to environmental violations and labor issues, Indonesia leveraged its export ban policies to demand compliance with domestic regulations, imposing \$124 million in fines and suspending operations of 15 facilities in 2022-2023 (Ministry of Environment 2024).

In contrast, Indonesia's engagement with the United States reflects a different modality of economic diplomacy, centered on expanding cooperation in technology, clean energy, innovation, and the digital sector. During 2014-2024, US investment in Indonesia totaled \$31.2 billion, concentrated in digital economy (\$8.4 billion), renewable energy (\$6.7 billion), healthcare (\$5.3 billion), and advanced manufacturing (\$4.9 billion) (BKPM 2024). Through partnerships with US technology firms including Google, Microsoft, Amazon Web Services, and Apple, Indonesia gained access to cloud computing infrastructure investments worth \$8.2 billion, data center construction supporting 2.1 gigawatts of capacity, digital skills training programs reaching 3.2 million participants, and technology transfer agreements covering AI, cybersecurity, and digital payments (Ministry of Communication and IT 2024).

Enhanced maritime and defense collaboration complemented economic partnerships, with US-Indonesia military cooperation expanding significantly: bilateral defense trade increased from \$42 million in 2014 to \$187 million in 2023; joint military exercises increased from 15 events in 2014 to 37 events in 2023; and maritime domain awareness cooperation involved installation of radar systems, patrol boat transfers, and intelligence sharing mechanisms valued at \$312 million cumulatively during 2014-2024 (US Department of Defense 2024). This demonstrates Indonesia's strategy of leveraging diversified economic relationships to access complementary benefits while maintaining political equidistance (Connelly 2015; Sukma 2019).

## 2. Indonesia's Integrated Economic Bandwagoning and Hedging Strategy

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Indonesia's strategic orientation under President Jokowi reflects a carefully engineered blend of selective economic bandwagoning with China and a broad hedging posture toward other major powers, with economic diplomacy functioning as the central instrument that binds these approaches together. Rather than aligning on ideological or security grounds, Indonesia leverages economic diplomacy to secure financing, economic development and cooperation; maritime, aerospace, *scientific and technological collaboration, along with socio-cultural partnership* that are essential for national development while navigating the pressures of the U.S.-China rivalry (Anwar 2023).

Its engagement with China illustrates this pragmatic diplomacy: Jakarta capitalizes on China's readiness to fund high-risk, capital-intensive projects including the Jakarta-Bandung high-speed rail, large-scale hydropower developments, and nickel smelting facilities to accelerate industrial upgrading and strengthen its downstream sectors (Medeiros 2005-06). Yet this engagement is tightly regulated through economic diplomatic tools such as export bans, technology transfer requirements, downstreaming policies, and local content rules, ensuring that Chinese investment contributes directly to national capacity-building rather than fostering dependency (Guberman, D., et al. 2024).

Complementing this bandwagoning, Indonesia simultaneously implements a hedging strategy through a diversified network of economic partnerships designed to counterbalance China's influence and maintain strategic autonomy. Economic diplomacy plays a decisive role as Indonesia expands targeted cooperation with the U.S., Japan, South Korea, India, Australia, as well as the European Union (BKPM 2023). Japan contributes high-standard infrastructure and industrial modernization; the United States supports Indonesia's digital economy, renewable energy initiatives, and data-center investment; South Korea deepens the electric-vehicle and battery ecosystem; while India and Australia expand maritime cooperation, supply chain diversification, and energy partnerships.

These dual pathways reveal that Indonesia's foreign economic strategy is not a contradictory amalgamation of policies but rather a coherent, diplomacy-driven framework. Indonesia negotiates financing terms to mitigate debt risks, uses regulatory leverage to secure long-term developmental gains, broadens its diplomatic ties to diversify economic options, and participates selectively in China's BRI and U.S.-led Indo-Pacific initiatives without committing exclusively to either (Kuik 2016). In doing so, economic diplomacy becomes the decisive instrument that transforms Indonesia from a passive object of great power rivalry into an active architect of its own developmental trajectory.

### 3. Case Studies: Empirical Evidence of Indonesia's Strategic Complementarity

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Indonesia's strategy of strategic complementarity becomes most visible when examined through concrete cases that demonstrate how economic diplomacy is operationalized amid intensifying U.S.-China rivalry.

*Case Study 1: High-Speed Rail Debt Renegotiation*

The Jakarta–Bandung rapid rail project project became a major test case for Indonesia's approach toward Chinese-funded infrastructure after substantial cost overruns pushed the government to renegotiate the project's debt structure. Indonesia did not simply accept the financial burden but instead entered formal negotiations with Beijing to restructure the terms of the loan, demonstrating a proactive stance in correcting unfavorable financial risks. The Indonesian government firmly refused the use of state funds (APBN) to cover the project's swelling debt, instead assigning repayment responsibilities to PT Danantara, ensuring that fiscal sovereignty remains protected. Indonesia sought to extend the loan maturity period to as long as 60 years to alleviate repayment pressure, an indication that Indonesia is negotiating from a position of strategic caution rather than passively accepting China's terms (Nabbs-Keller 2019).

*Case Study 2: Chinese Dominance in Nickel Refining*

Chinese companies hold around three-quarters of Indonesia's nickel processing capacity, which in turn prompts worries regarding potential economic overdependence. Nevertheless, this situation also reflects Indonesia's assertive industrial policy choices. Through measures such as the nickel export ban, the Indonesian government compelled Chinese firms to shift from raw material extraction to building smelters and refining facilities domestically, enabling Indonesia to increase domestic value creation and accelerate downstream industrialization (Warburton 2017). However, this proactive industrial policy does not eliminate risks associated with heavy reliance on Chinese capital, technology, and industrial ecosystems, including environmental challenges and structural dependencies, reinforcing the necessity of a hedging strategy (Lee and Hsieh 2022).

*Case Study 3: Strategic Diversification through India*

Indonesia's decision to deepen maritime and security cooperation with India represents a deliberate move to diversify its strategic partnerships beyond the traditional East Asian sphere dominated by China and U.S.-aligned actors. High-level meetings between the two countries have reaffirmed shared commitments to enhancing maritime domain awareness, strengthening naval cooperation, and expanding joint initiatives in defense production. By working with India, another major power wary of China's assertiveness, Indonesia broadens its spectrum of security relationships, reducing reliance on any single partner and reinforcing a multipolar foundation for regional order. This diversification serves multiple strategic purposes: it mitigates risks associated with Indonesia's deep economic integration

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with China, creates additional channels for defense collaboration, and supports Indonesia's commitment to maintaining an autonomous foreign policy posture (Shekhar and Liow 2014).

#### 4. Analysis of Strategic Outcomes and Challenges

##### *Successes and Achievements*

Indonesia's hedging strategy through economic diplomacy has achieved significant successes. First, Indonesia successfully attracted substantial investment from competing powers simultaneously. During 2014-2024, Indonesia received major investments from China, the United States, Japan, Australia, and other partners across diverse sectors, with total FDI inflows averaging over \$30 billion annually (BKPM 2023). Second, Indonesia maintained relatively strong economic growth despite regional uncertainties, with GDP growth averaging approximately 5 percent annually during the Jokowi period. Third, Indonesia preserved strategic autonomy and avoided pressure to choose sides definitively, maintaining constructive relationships with both powers (Roberts, Habir, and Sebastian 2015). Fourth, infrastructure development proceeded rapidly, addressing critical bottlenecks through major projects including the Jakarta MRT, numerous toll roads, new ports, and power generation capacity. Fifth, Indonesia enhanced its regional diplomatic standing by Indonesia should more explicitly connect economic diplomacy with defense industrial development by negotiating technology transfer for military equipment purchases, developing domestic defense manufacturing capabilities, pursuing joint development programs, and leveraging economic relationships to secure dual-use technologies (Nabbs-Keller 2019).

##### *Challenges and Vulnerabilities*

Despite these successes, Indonesia's hedging strategy faces significant challenges threatening long-term sustainability. First, intensifying pressure to choose sides emerges as US-China competition deepens structurally. During 2022-2024, both powers increasingly demanded clearer alignment from regional states through: US restrictions on Chinese technology requiring partner countries to choose between Chinese 5G systems and Western alternatives, affecting \$12.4 billion worth of Indonesian telecommunications infrastructure; Chinese economic pressure on countries participating in Quad activities, with reported delays in Chinese project approvals for Indonesia following participation in Quad Plus meetings; Technology export controls requiring source-country alignment, particularly affecting Indonesia's semiconductor aspirations requiring access to both Chinese markets and Western technology; and competing infrastructure standards creating incompatible systems, with Indonesia currently operating Chinese railway systems (Jakarta-Bandung HSR), Japanese urban transit (Jakarta MRT), and exploring US-backed digital infrastructure (USTR 2024; Ministry of Communication 2024).

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Second, debt sustainability concerns emerge from heavy infrastructure borrowing, though Indonesia maintains manageable levels compared to regional peers. Indonesia's external debt reached \$408.6 billion in 2023, representing 29.8% of GDP—below the 40% threshold typically considered risky but substantially higher than 25.2% in 2014 (World Bank 2024; Bank Indonesia 2024). Debt composition shows concentration risks, with Chinese creditors holding approximately 18.4% of external debt (\$75.2 billion), including: bilateral loans through China Development Bank and Export-Import Bank of China totaling \$28.7 billion, primarily for infrastructure projects; commercial borrowing by Indonesian SOEs from Chinese financial institutions totaling \$31.4 billion; and syndicated loans involving Chinese banks totaling \$15.1 billion (Ministry of Finance 2024).

Debt service obligations increased substantially, with annual external debt payments rising from \$31.8 billion in 2014 to \$57.3 billion in 2023, representing 4.2% of GDP, while debt service coverage ratios remained adequate at 3.8x, indicating manageable though growing pressure (Bank Indonesia 2024).

Third, technological dependence on China poses strategic vulnerabilities across multiple critical sectors. Chinese technology dominance in Indonesian digital infrastructure includes: telecommunications equipment market share of 67%, with Huawei and ZTE supplying majority of 4G/5G infrastructure valued at \$18.4 billion; nickel processing technology supplied by Chinese firms for 94% of Indonesian smelting capacity, representing technology dependencies worth \$12.7 billion; e-commerce platforms with Chinese ownership or technology (Shopee-Sea Group, Tokopedia with Alibaba investment, Lazada-Alibaba) capturing 73% of Indonesian e-commerce market worth \$62.4 billion in 2023; and digital payments systems with Chinese technology integration (including Alipay cooperation, WeChat Pay pilots) processing transaction values exceeding \$184 billion annually (Ministry of Communication 2024; Bank Indonesia 2024).

These dependencies create potential leverage points for political pressure, demonstrated by: data sovereignty concerns regarding data flows to Chinese servers, affecting 127 million Indonesian users of Chinese-affiliated platforms; cybersecurity risks, with 47 reported incidents of potential data breaches involving Chinese technology during 2019-2023; and technology sanctions vulnerability, where US restrictions on Chinese technology could affect 43% of Indonesia's digital infrastructure (National Cyber Agency 2024).

Fourth, domestic capacity limitations constrain Indonesia's ability to maximize benefits from foreign engagement. Key constraints include: bureaucratic inefficiencies, with World Bank's Ease of Doing Business ranking Indonesia 73rd globally in 2023, below Malaysia (12th), Thailand (21st), and Vietnam (70th); regulatory unpredictability, with frequent revisions to investment regulations creating uncertainty—146 regulatory changes affecting foreign investment during 2014-2023;

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skills gaps limiting effective technology absorption, with OECD assessments indicating Indonesian workforce skills lagging regional competitors by 3-5 years in technical sectors; and infrastructure bottlenecks beyond major Java corridor, with logistics costs averaging 24% of product value compared to 14% regional average (World Bank 2024; OECD 2024).

Fifth, environmental and social costs of rapid development create domestic opposition that complicates foreign investment management. Key challenges include: coal-fired power plants contributing to air pollution, with 37 Chinese-financed coal plants generating 23.8 gigawatts capacity but causing estimated 7,800 premature deaths annually according to environmental studies; nickel mining expansion generating environmental degradation including deforestation of 47,300 hectares during 2019-2023, water pollution affecting 23 river systems, and displacement of 14,700 indigenous community members; and labor issues at foreign-invested facilities, with 284 labor disputes involving Chinese companies during 2019-2023, addressing wage violations, safety conditions, and union rights (Ministry of Environment 2024; ILO 2024).

Sixth, escalation risks in great power conflict pose existential threats to hedging strategy sustainability. Potential conflict over Taiwan would force impossible choices and disrupt economic ties with both powers, with estimated impacts including: trade disruption affecting \$165.7 billion in annual Indonesia-China trade and \$37.6 billion Indonesia-US trade; investment flows potentially declining 60-80% during conflict period based on historical precedents; supply chain disruption affecting critical inputs for Indonesian manufacturing, with 43% of intermediate goods sourced from potential conflict zones; and security pressures forcing alignment decisions that would fundamentally compromise hedging strategy viability (CSIS 2024; Lowy Institute 2024).

These challenges collectively threaten the sustainability of Indonesia's hedging approach, particularly as US-China competition shows little sign of abating and may intensify further in coming years (Goldstein 2020; Green et al. 2017).

## **CONCLUSION**

This research demonstrates that Indonesia's economic diplomacy amid intensifying US-China competition is fundamentally driven by a sophisticated hedging strategy designed to secure maximum economic advantage while maintaining strategic autonomy. Rather than aligning with either power, Indonesia strategically broadens its economic partnerships, using diplomacy to attract diverse sources of trade, investment, infrastructure financing, and technological cooperation.

Through soft balancing, Indonesia strengthens economic as well as technological linkages to the United States, Japan, Australia, and India, expanding investment channels, developing strategic industrial collaborations, and adopting

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alternative digital and infrastructure standards that reduce overdependence on China. These partnerships not only provide competitive financing and technology options but also enhance Indonesia's economic resilience and bargaining leverage. At the same time, Indonesia engages in economic bandwagoning by intensifying its targeted cooperation with China, especially through China's Belt and Road program, large-scale downstream nickel investments, industrial parks, and digital economy expansion. Chinese capital remains indispensable for financing mega-infrastructure projects, accelerating industrial upgrading, and sustaining Indonesia's export competitiveness.

The hedging framework illuminates Indonesia's signature blend of economic pragmatism, diversification, institutional participation, and calibrated security cooperation that avoids formal alliances. Empirical evidence across policy documents, speeches, investment statistics, and project records confirms Indonesia's success in securing capital from multiple major powers, diversifying infrastructure financing, and expanding both Chinese and non-Chinese economic engagements. Overall, Indonesia's economic diplomacy has been highly effective in attracting investment, accelerating infrastructure development, supporting industrial transformation, and preserving strategic flexibility. Yet, its sustainability faces emerging pressures including US-China demands to choose sides, risks of debt and technological dependence, domestic capacity constraints, and escalating regional tensions.

#### *Policy Recommendations*

Indonesia's decade-long experience navigating US-China competition through economic diplomacy offers important lessons for policymakers both domestically and in other middle-power states facing similar strategic dilemmas. The most critical priority involves strengthening domestic capabilities that enable more effective leverage of external partnerships and greater resilience against external pressures. Bureaucratic reform remains essential to improve policy coordination across ministries, as fragmented decision-making has resulted in conflicting signals to foreign partners and delayed project implementation—the average approval time for major foreign investments stands at 18 months compared to 6-9 months in regional competitors like Vietnam and Thailand. Investment in human capital development through educational improvement, particularly in technical and engineering fields, proves crucial as current skills gaps limit Indonesia's capacity to absorb advanced technology transfers, with only 23% of Indonesian workers possessing technical qualifications compared to 41% in Malaysia and 38% in Thailand. Technological capacity building through increased research and development investment, currently at just 0.28% of GDP compared to regional average of 1.2%, would reduce dependency on foreign technology and enhance negotiating leverage. Strengthening institutional oversight mechanisms, particularly for debt management, environmental protection,

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and labor standards, would reduce vulnerabilities while maintaining Indonesia's attractiveness for responsible foreign investment.

Further economic diversification remains necessary beyond existing achievements to reduce concentration risks that could become leverage points for external pressure. Sectoral diversification beyond natural resource exports, which still comprised 47% of total exports in 2023, would reduce vulnerability to commodity price fluctuations and external demand shocks—priority sectors include digital services, creative industries, tourism, and high-value manufacturing where Indonesia possesses comparative advantages but remains underexploited. Geographic diversification by expanding engagement with middle powers including South Korea, UAE, Saudi Arabia, and EU countries would reduce dependency on any single major power—these partners often provide technology transfers and financing with fewer geopolitical strings attached than US or Chinese alternatives. Supply chain diversification by developing domestic supplier capabilities remains critical, as current reliance on imported intermediate goods representing 43% of manufacturing inputs creates vulnerabilities to external supply disruptions—policies supporting small and medium enterprise development in supply chain roles would enhance resilience. Financial diversification through capital market development, expanding bond market depth and reducing reliance on foreign currency debt, would minimize exposure to external financial shocks—currently 68% of Indonesian external debt is denominated in US dollars, creating exchange rate vulnerabilities.

Indonesia should develop more sophisticated economic statecraft capabilities to protect national interests while remaining open to beneficial foreign engagement. Investment screening mechanisms similar to the U.S. Committee on Foreign Investment (CFIUS) or Australia's Board for Reviewing Foreign Investments would enable systematic assessment of national security implications without creating perception of general investment hostility—current Indonesian screening processes remain ad hoc and inconsistent. Enhanced due diligence for infrastructure financing, including comprehensive debt sustainability analyses, environmental impact assessments, and technology dependency evaluations before project approval, would prevent problematic commitments that later require costly renegotiation. Data sovereignty regulations establishing clear rules for data localization, cross-border data flows, and foreign access to sensitive data would protect Indonesian citizens and businesses while providing predictability for foreign technology companies—current regulatory ambiguity creates both security risks and investment uncertainty. Technology transfer requirements that are transparent, reasonable, and consistently enforced would maximize developmental benefits from foreign investment without deterring participation—current requirements, while extensive on paper, often go unenforced due to weak monitoring capacity. Strategic stockpiling of critical resources including food staples, energy supplies, medical equipment, and industrial inputs

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would provide a buffer against external supply disruptions during geopolitical crises—Indonesia's current strategic reserves remain limited compared to countries like Japan or South Korea that maintain multi-month supplies of critical goods.

As ASEAN's largest economy representing 36% of regional GDP, Indonesia should invest more heavily in strengthening regional institutions that amplify middle-power influence and constrain great power unilateralism. Revitalizing ASEAN economic integration through acceleration of regional comprehensive economic partnership implementation, digital economy integration, and supply chain connectivity would increase the collective bargaining power of Southeast Asian states—ASEAN's combined GDP of \$3.6 trillion represents significant market leverage when acting cohesively. Strengthening ASEAN's function in regional security governance framework by strengthening ASEAN Defense Ministers' Meeting Plus, expanding practical security cooperation, and developing ASEAN's capacity for conflict prevention and crisis management would provide alternatives to great power-led security frameworks—current ASEAN security mechanisms remain consultative rather than operational, limiting effectiveness. Promoting ASEAN centrality in emerging issue areas including digital governance, climate change, public health, and maritime security would ensure regional priorities shape rule-making rather than having external standards imposed—ASEAN has successfully established norms in traditional security areas but lags in newer domains. Building coalitions with like-minded middle powers beyond Southeast Asia, including Australia, South Korea, India, UAE, and progressive EU members, would create alternative partnerships that reduce dependence on major powers while advancing shared interests in open, rules-based regional order—Indonesia's current middle-power diplomacy remains underutilized compared to its potential influence.

Indonesia should more explicitly connect economic diplomacy with defense industrial development to reduce security dependencies while building domestic capabilities with commercial applications. Negotiating technology transfer requirements for military equipment purchases, rather than simply procuring finished systems, would accelerate domestic defense industry development—current procurement often involves minimal technology transfer, limiting developmental benefits. Developing domestic defense manufacturing capabilities through public-private partnerships, research and development support, and integration of defense industries with commercial manufacturing sectors would create dual-use capabilities enhancing both security and economic competitiveness—Indonesia's defense industry currently meets only 34% of domestic military requirements. Pursuing joint development programs with multiple international partners for specific capabilities including maritime patrol aircraft, armored vehicles, precision munitions, and radar systems would diversify technology sources while building domestic expertise—current Indonesian defense partnerships remain limited to handful of suppliers.

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Leveraging economic relationships to secure dual-use technologies applicable to both civilian and military purposes, including satellite systems, cybersecurity capabilities, advanced materials, and artificial intelligence applications, would enhance national capabilities while avoiding perception of military buildup—strategic use of economic leverage could accelerate access to technologies often restricted through security export controls.

Given escalation risks in US-China competition that could force impossible alignment choices, Indonesia should develop contingency plans enabling maintenance of core interests across various scenarios. Identifying critical relationships to preserve if forced to prioritize, Indonesia should determine which partnerships prove absolutely essential for economic development, food security, energy security, and defense capabilities under different conflict scenarios—advance identification would enable rapid decision-making during crises. Establishing crisis management mechanisms including interagency coordination systems, communication channels with major powers, and diplomatic strategies for various contingencies would improve Indonesia's capacity to respond effectively to rapid escalation—current crisis management capacity remains limited and reactive. Building economic resilience through increased self-sufficiency in food production, energy supply, critical minerals processing, and essential manufacturing would reduce vulnerability to external supply disruptions during geopolitical crises—Indonesia possesses resources for substantial self-sufficiency but requires sustained investment and policy support. Developing diplomatic pathways for managing various escalation scenarios, including regional conflict, economic sanctions, technology restrictions, and supply chain disruptions, would enable Indonesia to maintain maximum autonomy even under severe external pressure—scenario planning and strategy development should occur during peacetime rather than improvising during crises.

Indonesia should improve strategic communication of its hedging logic to domestic and international audiences, reducing misunderstandings that could complicate implementation. Domestically, explaining how hedging serves national interests by maintaining independence, maximizing economic benefits, and avoiding entanglement in great power conflicts would build public support for occasionally uncomfortable policy positions—current public debate often mischaracterizes hedging as indecisiveness rather than strategy. Internationally, articulating Indonesia's approach as principled non-alignment rooted in national experience and regional stability rather than opportunistic fence-sitting would manage expectations and reduce pressure from major powers—clear communication of strategic logic helps partners understand Indonesian positions even when they disagree. Developing consistent messaging across government institutions, ensuring all ministries and agencies communicate compatible explanations of Indonesian strategy, would reduce contradictory signals that create confusion and opportunities for external

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exploitation—current fragmented communications sometimes undermine strategic coherence.

These recommendations collectively aim to enhance Indonesia's capacity to maintain strategic autonomy through economic diplomacy while preparing for potential scenarios where hedging becomes more difficult or impossible. Implementation requires sustained political commitment, bureaucratic capacity building, and resource allocation, but would significantly strengthen Indonesia's position in an increasingly contested regional environment.

### *Final Reflection*

Indonesia's economic diplomacy strategy represents a sophisticated attempt by a significant middle power to navigate great power competition while advancing national development objectives. The approach reflects both principled commitments rooted in Indonesia's non-aligned foreign policy tradition and pragmatic recognition of contemporary power realities. By actively engaging all major powers simultaneously, Indonesia has secured substantial economic benefits while preserving strategic autonomy that many observers believed would prove impossible to maintain as US-China competition intensified.

However, the strategy's sustainability faces growing challenges as competition deepens and pressure for alignment increases. The fundamental question facing Indonesia and other middle powers is whether skilled diplomacy can indefinitely navigate between competing great powers or whether intensifying rivalry will eventually force impossible choices. Historical precedent suggests skepticism about long-term hedging sustainability during great power conflicts, yet historical circumstances also differ significantly from contemporary conditions including economic interdependence depth, nuclear deterrence, and international institutional development.

For now, Indonesia's economic diplomacy stands as testimony to the possibilities of strategic autonomy through active engagement, sophisticated balancing, and principled commitment to multilateral order. Whether this approach proves sustainable depends not only on Indonesian skill but also on whether great powers ultimately accept limits on their competition or instead demand the exclusive alignments that would destroy the regional architecture Indonesia and its neighbors have worked decades to build.

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