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NAVIGATING REGIONAL COMPETITION: THE COMPETITIVENESS OF INDONESIA'S MSMES IN THE ASEAN MARKET

Lini Ingriyani¹, Rizki Marman Saputra²

¹Accounting, Politeknik Negeri Jakarta, Indonesia

²Graduate School of Sustainable Development, Universitas Indonesia, Indonesia

lini.ingriyani@akuntansi.pnj.ac.id¹, rizki.marman11@ui.ac.id²

Abstract

The establishment of the ASEAN Economic Community (AEC) marks a significant milestone in Southeast Asia's regional integration efforts, driving economic liberalization, free trade, and cross-border investment flows. Within this dynamic regional environment, Indonesia's Micro, Small, and Medium Enterprises (MSMEs)—which serve as the backbone of the national economy—face both vast opportunities and complex challenges. This study explores how ASEAN's economic liberalization has opened new market access, strengthened technological collaboration, and fostered cross-border investment linkages, while simultaneously intensifying competition among enterprises across member states. Using liberalism theory in international relations as an analytical framework, this research argues that ASEAN's economic interdependence produces a dual effect: on one hand, it enhances growth potential through cooperation, but on the other, it exposes structural weaknesses among MSMEs that lack competitiveness. Furthermore, this study examines the institutional role of ASEAN, particularly in enhancing MSME competitiveness through policy harmonization, capacity building, and digital transformation initiatives. Through mechanisms such as best-practice sharing and policy benchmarking, ASEAN institutions contribute to narrowing development gaps among member states and supporting inclusive regional growth. The findings highlight that the competitiveness of Indonesia's MSMEs in the ASEAN market is determined not only by domestic innovation and efficiency but also by the collective institutional strength of ASEAN in promoting a balanced, open, and cooperative regional economy.

Keywords: ASEAN Economic Community, MSME competitiveness, economic liberalization, regional interdependence, Indonesia's MSMEs

Abstrak

Pembentukan Masyarakat Ekonomi ASEAN (MEA) menandai tonggak penting dalam upaya integrasi kawasan Asia Tenggara, yang mendorong liberalisasi ekonomi, perdagangan bebas, serta arus investasi lintas negara. Dalam lingkungan regional yang dinamis ini, Usaha Mikro, Kecil, dan Menengah (UMKM) Indonesia—sebagai tulang punggung perekonomian nasional—menghadapi peluang yang besar sekaligus tantangan yang kompleks. Penelitian ini mengkaji bagaimana liberalisasi ekonomi ASEAN telah membuka akses pasar baru, memperkuat kolaborasi teknologi, dan mendorong keterkaitan investasi lintas negara, namun pada saat yang sama juga meningkatkan intensitas persaingan antar pelaku usaha di negara-negara anggota. Dengan menggunakan teori liberalisme dalam hubungan internasional sebagai kerangka analisis, penelitian ini berargumen bahwa interdependensi ekonomi ASEAN menghasilkan dampak ganda: di satu sisi, meningkatkan potensi pertumbuhan melalui kerja sama, tetapi di sisi lain, menyingkap kelemahan struktural UMKM yang belum memiliki daya saing yang memadai. Lebih lanjut, penelitian ini menelaah peran kelembagaan ASEAN, khususnya dalam meningkatkan daya saing UMKM melalui harmonisasi kebijakan, penguatan kapasitas, dan inisiatif transformasi digital. Melalui mekanisme seperti pertukaran praktik terbaik (*best-practice sharing*) dan *policy benchmarking*, institusi ASEAN berkontribusi dalam mempersempit kesenjangan pembangunan antarnegara anggota serta mendukung pertumbuhan kawasan yang inklusif. Temuan penelitian menunjukkan bahwa daya saing UMKM Indonesia di pasar ASEAN tidak hanya ditentukan oleh inovasi dan efisiensi domestik, tetapi juga oleh kekuatan kelembagaan kolektif ASEAN dalam mendorong terciptanya perekonomian kawasan yang seimbang, terbuka, dan berbasis kerja sama.

Kata kunci: Masyarakat Ekonomi ASEAN, daya saing UMKM, liberalisasi ekonomi, interdependensi regional, UMKM Indonesia

I. INTRODUCTION

In the era of economic globalization, regional integration has become a crucial strategy for countries to enhance growth, stability, and collective competitiveness. Southeast Asia, through the establishment of the ASEAN Economic Community (AEC), embodies this spirit of cooperation by promoting free trade, investment mobility, and economic collaboration among its member states. The AEC's vision to create a single market and production base aims to strengthen ASEAN's position in the global economy while fostering inclusive growth within the region. Within this framework, Micro, Small, and Medium Enterprises (MSMEs) play a central role as the backbone of national economies, particularly in Indonesia, where this sector contributes significantly to employment, Gross Domestic Product (GDP), and social development (ASEAN Secretariat, 2015).

Indicator	Value / Fact	Notes / Sources
Total number of MSMEs in Southeast Asia	≥ 70 million	ASEAN states 70 million MSMEs (ASEAN Secretariat)
Proportion of MSMEs in total ASEAN enterprises	> 99%	The SME Policy Index ASEAN 2024 states that MSMEs account for more than 99% of all registered enterprises across ASEAN member states. (ASEAN Secretariat)
Digitalization and policy trends	Increased policy support, digital transformation, and focus on sustainable growth	The SME Policy Index 2024 highlights that ASEAN members are strengthening their digitalization and sustainability policies to accelerate MSME development. (SNRD Asia)
MSME data and digital export surveys	Indonesia and other ASEAN countries are included in digital export research	The MSMEs Digital Export in Southeast Asia (2022) study sampled MSMEs from Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam. (International Chamber of Commerce (ICC))
Role of MSMEs in Asia (overall)	> 96% of all businesses, providing about two-thirds of private-sector employment	According to ADB Institute (Yoshino & Taghizadeh-Hassary), MSMEs account for more than 96% of all enterprises and contribute roughly two-thirds of private-sector employment across Asia. (ResearchGate)

Figure 1. An overview of the Micro, Small, and Medium Enterprise (MSME) market in Southeast Asia

From the table above, it can be seen that the MSME market in Southeast Asia represents a vital and dynamic economic sector. According to data from the Asian Development Bank (ADB, 2020), there are at least 71 million MSMEs in the region, accounting for around 97% of all enterprises and serving as the backbone of the ASEAN economy. The ASEAN SME Policy Index 2024 report further emphasizes that MSMEs constitute more than 99% of registered business entities, highlighting their dominant role in regional economic growth. In line with this, ASEAN

member states are increasingly strengthening policies on digitalization and sustainability to enhance MSME competitiveness, including promoting digital exports as noted in the ICC (2022) study. More broadly across Asia, the ADB Institute reports that MSMEs account for over 96% of businesses and provide about two-thirds of private sector employment, reaffirming their strategic role in driving inclusive and sustainable economic growth.

However, behind this significant contribution, the increasingly open regional market dynamics bring their own set of consequences. Market liberalization and the growing economic interdependence within the region present new challenges for ASEAN MSMEs, including those in Indonesia. Intensifying competition among member states requires businesses to adapt more swiftly to changes in market structures and technological advancements. In this context, Indonesian MSMEs are no longer competing solely in the domestic arena but also at the regional level, facing competitors from Malaysia, Thailand, and Vietnam, which possess more mature industrial ecosystems and stronger export capabilities. This situation underscores the urgent need for Indonesian MSMEs to undergo transformation—becoming more adaptive, innovative, and digitally oriented—to sustain their competitiveness in the ASEAN market (Chia, 2013; Dent, 2008).

On the other hand, these challenges also present significant strategic opportunities. Through ASEAN's regional economic integration under the framework of the ASEAN Economic Community (AEC), Indonesian MSMEs have the opportunity to expand market access, strengthen cross-border production networks, and benefit from the facilitation of intra-ASEAN investment and trade (Severino & Menon, 2017). Nevertheless, this vast potential is often overshadowed by structural

constraints such as limited access to financing, technological gaps, and regulatory barriers that continue to hinder competitiveness enhancement (OECD, 2018).

To comprehend the complexity of these opportunities and challenges, liberalism in international relations provides a relevant analytical framework. This theory posits that states can achieve shared prosperity through economic cooperation and institutional interdependence, rather than solely through power rivalry (Keohane & Nye, 1977; Moravcsik, 1997). Using this perspective, this paper analyzes how ASEAN's economic integration—grounded in the principles of market liberalization and free trade—affects the competitiveness of Indonesian MSMEs. The analysis also highlights how regional interdependence influences business behavior, national policy adjustments, and cross-border collaboration within the ASEAN market.

Overall, this study seeks to examine the dynamic interrelation between regional economic liberalization, economic interdependence, and the competitiveness of Indonesian MSMEs within the ASEAN market context. By navigating regional competition through the lens of liberalism, this paper underscores the dual nature of ASEAN integration: as both an opportunity for growth and a challenge to domestic economic resilience. Understanding this balance is crucial for formulating policy strategies and empowerment models that can enhance the competitive advantage of Indonesian MSMEs, enabling them to participate actively and sustainably in the evolving regional economic landscape.

II. THEORETICAL FRAMEWORK

The liberalism theory in international relations emphasizes that interactions among states are not solely focused on power and security, as assumed by realism,

but rather on the potential for mutually beneficial cooperation through international institutions, free trade, and economic interdependence (Keohane & Nye, 1977; Moravcsik, 1997). Liberalism posits that by strengthening economic relations and building trust among nations, stability and shared prosperity can be achieved. In the context of Southeast Asia, this perspective underpins the establishment of various regional cooperation mechanisms, including the ASEAN Economic Community (AEC), which seeks to integrate the economies of ASEAN member states through market liberalization, the removal of trade barriers, and the enhancement of the mobility of goods, services, and investments (Nesadurai, 2003; Severino & Menon, 2017).

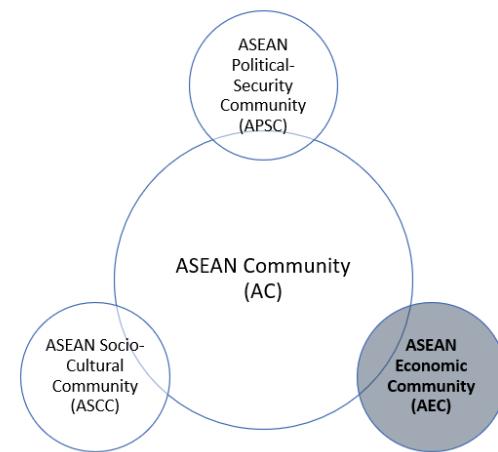


Figure 2. Three Pillars of ASEAN Community

ASEAN's economic integration through the AEC represents a concrete manifestation of liberal values in the form of institutionalized regional economic cooperation. This mechanism plays a pivotal role in creating a single market and integrated production base, strengthening the region's economic competitiveness, and fostering inclusive and sustainable growth. Through trade and investment liberalization, the AEC has deepened economic linkages among ASEAN member

states, creating conditions in which the economy of one country influences—and is influenced by—others. This phenomenon is known as *economic interdependence*, referring to the reciprocal economic dependence among member countries (Dent, 2008; Chia, 2013).

The regional economic interdependence emerging from AEC integration has direct implications for businesses in the region, particularly for Micro, Small, and Medium Enterprises (MSMEs) in Indonesia. Market liberalization offers MSMEs the opportunity to expand their business reach within the ASEAN market by improving access to distribution networks, technology, and cross-border financing. On the other hand, an open market also brings challenges in the form of heightened competition from businesses in other member states with higher efficiency and competitiveness. Consequently, the competitiveness of Indonesian MSMEs is determined not only by internal capabilities—such as innovation, cost efficiency, and product quality—but also by external factors, including the dynamics of regional economic policies and the level of ASEAN market integration.

Thus, the relationship between liberalism theory, ASEAN economic integration, and the competitiveness of Indonesian MSMEs can be understood as an interconnected conceptual framework. Liberalism provides the normative foundation emphasizing the importance of cooperation and free trade; the AEC functions as the regional institution that operationalizes these principles; and the resulting economic interdependence creates both competitive and collaborative environments for Indonesian MSMEs to enhance their competitiveness in the ASEAN market. From this perspective, it can be concluded that the competitiveness of Indonesian MSMEs is the outcome of an institutionalized economic liberalization

process through the AEC, where regional cooperation acts as a catalyst in strengthening economic interconnectedness and promoting sustainable development across Southeast Asia.

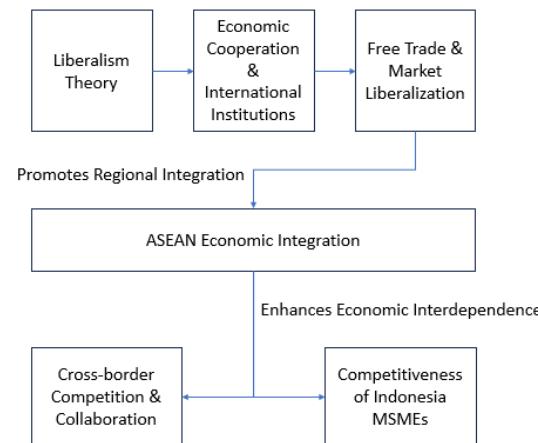


Figure 3. Linkage between Liberalism Theory, ASEAN Economic Integration, and the Competitiveness of Indonesian MSMEs

The graph above is a conceptual illustration depicting the relationship between Liberalism Theory, ASEAN Economic Integration (AEC), and the Competitiveness of Indonesian MSMEs. The diagram demonstrates how economic cooperation and market liberalization foster regional economic interdependence, which ultimately influences the competitiveness of Indonesian MSMEs within the ASEAN market.

III. METHODS

This study employs a qualitative approach to comprehensively examine the dynamics of ASEAN's economic liberalization and its impact on the competitiveness of Indonesian MSMEs within the context of regional economic integration. This approach was chosen because it allows for a contextual understanding of the meanings, processes, and relationships among policy and institutional variables that influence patterns of competition and economic collaboration at the regional level

(Creswell, 2014). Through this approach, the study seeks to interpret how the principles of economic liberalism are reflected in ASEAN's policies, and how regional institutions such as the ASEAN SME Policy Index contribute to strengthening the capacity and competitiveness of MSMEs among ASEAN member states.

The data used in this study are entirely derived from secondary sources that hold high relevance and credibility to the topic under investigation. The primary sources include policy documents such as the *ASEAN Economic Community (AEC) Blueprint 2025*, the *ASEAN SME Policy Index 2018* (OECD, ERIA & ASEAN, 2018), and annual reports from the ASEAN Secretariat. In addition, the study refers to publications from international organizations such as the Asian Development Bank (ADB), the Organisation for Economic Co-operation and Development (OECD), and the Economic Research Institute for ASEAN and East Asia (ERIA), which highlight issues of competitiveness and MSME policy in Southeast Asia. Other sources analyzed include reports from the Indonesian Ministry of Cooperatives and SMEs, as well as academic journal articles discussing economic liberalization, regional integration, and MSME competitiveness enhancement strategies. The selection of sources was conducted purposively, considering their relevance to the implementation period of the *AEC Blueprint 2025* and their connection to regional economic integration issues.

Data analysis was conducted through document analysis, following the interactive model of Miles, Huberman, and Saldaña (2014), which consists of three main stages. The first stage is *data reduction*, involving the selection and categorization of information from various documents based on themes such as

economic liberalization, ASEAN integration policy, institutional roles, and MSME competitiveness strategies. The second stage is *data display*, carried out by developing thematic matrices and conceptual maps to identify patterns of relationships among variables and detect regional policy trends. The third stage is *conclusion drawing and verification*, which involves interpreting data through iterative reading, theoretical reflection, and comparison with relevant literature to ensure the consistency and validity of interpretations.

To ensure the credibility and validity of the analysis, several validation strategies were applied. *Source triangulation* was conducted by comparing findings across documents from various regional and international institutions to obtain a comprehensive and accurate picture. *Peer debriefing* sessions with academics and researchers in the field of international political economy were also used to minimize interpretative bias and strengthen analytical objectivity. Additionally, the researcher implemented an *audit trail*—a systematic record of the analytical process, thematic categorization, and interpretive steps—to ensure transparency and scientific accountability.

This study is limited to examining the policy and institutional context of ASEAN's economic liberalization during the implementation period of the *AEC Blueprint 2025*. The analysis focuses on the dimensions of regional cooperation, institutional capacity building, and their implications for the competitiveness of Indonesian MSMEs in the ASEAN market. Quantitative aspects, such as financial performance or export data, are not the main focus. Accordingly, this study aims to provide a conceptual contribution to the understanding of the relationship between economic liberalization, the role of ASEAN institutions, and the strengthening of

MSME competitiveness within the framework of regional economic cooperation.

IV. ASEAN ECONOMIC LIBERALIZATION AND REGIONAL INTEGRATION

Economic liberalization in Southeast Asia marks a pivotal milestone in shaping ASEAN's economic identity as an interconnected and competitive region. Through the establishment of the ASEAN Economic Community (AEC) in 2015, member states committed to creating a *single market and production base* that enables the free flow of goods, services, investment, skilled labor, and capital (ASEAN Secretariat, 2015). This liberalization process not only reflects an economic transformation but also embodies the core principles of international economic liberalism, which emphasize market openness, institutional cooperation, and economic interdependence as pathways to shared prosperity (Keohane & Nye, 1977; Moravcsik, 1997).

Unlike the European Union's model of economic integration, ASEAN adopts a gradual and consensus-based approach known as the *ASEAN Way*. This approach prioritizes national sovereignty over strict policy harmonization while fostering trust and economic connectivity among member states. This can be observed in various liberalization initiatives, such as the *ASEAN Trade in Goods Agreement (ATIGA)* and the *ASEAN Comprehensive Investment Agreement (ACIA)*, which have reduced tariff barriers and strengthened intra-ASEAN investment flows (Chia, 2013; Severino & Menon, 2017). Although progress has been incremental, ASEAN's liberalization has gradually transformed the region's economic structure—from one rooted in protectionism to one characterized by openness and deeper integration.

In Indonesia's context, ASEAN's economic liberalization presents both opportunities and challenges. On the one hand, regional market openness provides opportunities for Indonesian MSMEs to expand export reach, establish cross-border distribution networks, and gain access to production resources and foreign investment (OECD, ERIA & ASEAN, 2018). Through trade and investment liberalization, MSMEs can integrate into regional value chains, thereby strengthening their position within the global economic system (Dent, 2008; ADB, 2020). Moreover, ASEAN integration policies have opened avenues for knowledge transfer, managerial capacity building, and the adoption of higher production standards—all of which can enhance the efficiency and productivity of Indonesia's MSME sector.

However, economic liberalization also brings significant challenges. Increased trade and investment flows have intensified competition, especially for MSMEs that lack comparable price competitiveness, product quality, and innovation to match enterprises from other ASEAN members such as Malaysia, Thailand, and Vietnam (Nesadurai, 2003; OECD, 2019). Additional challenges arise from persistent structural and regulatory disparities across ASEAN countries—including gaps in digital infrastructure, access to finance, and human capital readiness. These inequalities mean that liberalization does not always produce equitable benefits across member states, including Indonesia, which, despite having a large MSME base, continues to face limitations in technological adoption and competitiveness.

In this context, ASEAN's institutional role becomes increasingly crucial. Institutions such as the *ASEAN SME Policy Index* serve as regional policy instruments to assess, monitor, and strengthen the effectiveness of MSME-related policies in member states (OECD, ERIA & ASEAN, 2018). Through

this index, member countries can conduct policy benchmarking and share best practices in areas such as innovation, digitalization, access to finance, and entrepreneurship development. This approach aligns with the principles of *institutional liberalism*, wherein cooperation among states is facilitated through institutions to reduce uncertainty and enhance economic coordination (Keohane, 1984). Thus, ASEAN liberalization is not merely about removing trade barriers but also about building an institutional framework that ensures inclusiveness.

Aspect	Opportunities	Challenges	Institutional Role (ASEAN Mechanisms)	References
Market Access	Broader access to ASEAN regional markets through tariff reduction and trade facilitation.	Intense competition with MSMEs from Malaysia, Thailand, and Vietnam that have more advanced production systems.	ASEAN Trade in Goods Agreement (ATIGA) – eliminates tariff and non-tariff barriers to enhance intra-ASEAN trade.	ASEAN Secretariat (2015); Chia (2013); Severino & Menon (2017).
Investment and Capital Flow	Opportunities for cross-border investment and partnership with regional investors; potential access to foreign funding.	Limited financial literacy and access to cross-border financing mechanisms for small enterprises.	ASEAN Comprehensive Investment Agreement (ACIA) – promotes investment facilitation and protection across member states.	OECD, ERIA & ASEAN (2018); ADB (2020).
Technology and Innovation	Knowledge and technology transfer through regional cooperation and supply chain integration.	Technological gaps and low adoption of digital tools among MSMEs, particularly outside Java.	ASEAN SME Policy Index – assesses national policies to support MSME innovation, digitalization, and productivity.	OECD, ERIA & ASEAN (2018); ERIA (2021).
Regulatory Environment	Policy harmonization across ASEAN creates clearer standards for trade, certification, and quality assurance.	Differences in national regulations, bureaucratic barriers, and lack of standardization slow business expansion.	AEC Blueprint 2025 – sets framework for regulatory coherence and institutional alignment.	ASEAN Secretariat (2015); Dent (2008).
Human Capital and Skills	Regional training programs and ASEAN SME Academy enhance entrepreneurial skills and management capacity.	Uneven human resource distribution across regions; limited participation in ASEAN capacity-building programs.	ASEAN SME Academy and ASEAN Coordinating Committee on MSMEs (ACCMSME) – facilitate MSME education and networking.	OECD (2019); ADB (2020).
Regional Value Chains (RVCs)	Integration into ASEAN and global value chains increases competitiveness and export potential.	Low participation due to limited productivity, logistics inefficiency, and export readiness.	ASEAN Connectivity Master Plan (MPAC) – improves logistics, connectivity, and trade infrastructure.	Dent (2008); ADB (2020).
Institutional Coordination	ASEAN institutions provide frameworks for collaboration, data sharing, and policy benchmarking.	Policy implementation gaps at national level hinder regional alignment and benefit distribution.	ASEAN SME Policy Index & ASEAN Economic Ministers Meetings (AEM) – monitor implementation and progress of MSME policies.	Keohane (1984); OECD, ERIA & ASEAN (2018).

Figure 4. Comparison of Opportunities and Challenges of ASEAN Economic Liberalization for Indonesian MSMEs

The table above illustrates that ASEAN's economic liberalization has a dual effect on Indonesian MSMEs. On one hand, it creates opportunities for market expansion, increased investment, and technology transfer through regional cooperation mechanisms. On the other hand, it presents challenges in the form of intensified competition, technological disparities, and regulatory barriers that remain insufficiently harmonized at both national and regional levels. The role of ASEAN institutions—particularly through the *ASEAN SME Policy Index* and the *AEC Blueprint 2025*—is therefore crucial in balancing these effects of liberalization to

ensure inclusive and sustainable growth for MSMEs across the region.

For Indonesia, optimizing the role of ASEAN institutions requires aligning national policies with regional integration agendas. Strategies such as enhancing digital literacy, providing innovation incentives for export-oriented MSMEs, and strengthening cross-country collaboration in capacity development are essential for navigating the dynamics of an open market. With strong institutional support, ASEAN's economic liberalization has the potential to serve as a catalyst for accelerating structural transformation and reinforcing national economic resilience through MSME empowerment.

Conceptually, ASEAN's economic liberalization underscores a reciprocal relationship between market openness and institutional capacity building. Liberalization that is not accompanied by adaptive policymaking and institutional strengthening may widen competitiveness gaps among member states. Conversely, when national and regional policies are aligned in supporting MSMEs, liberalization can act as a driving force for sustainable and inclusive economic integration. In Indonesia's case, success in facing regional competition will depend greatly on the government's and business actors' ability to leverage ASEAN integration as an opportunity for capacity enhancement—rather than viewing it merely as a threat to domestic economic stability.

V. THE ROLE OF ASEAN INSTITUTIONS

The institutional structure of ASEAN serves as a fundamental mechanism that bridges the process of regional economic liberalization with tangible policy implementation that delivers direct benefits to businesses, including MSMEs in Indonesia. Conceptually, the *ASEAN*

Economic Community (AEC) Blueprint 2025 mandates the establishment of a single market and production base supported by regulatory harmonization and MSME capacity strengthening across all member states (ASEAN Secretariat, 2015). However, the effectiveness of this mandate largely depends on how well ASEAN institutions can coordinate policies, reduce cross-border transaction costs, and enhance the capabilities of micro and small enterprises.

In practice, there are three institutional pathways within ASEAN that play significant roles in shaping the MSME ecosystem. First, *rule-making and market access enhancement* through agreements such as the *ASEAN Trade in Goods Agreement (ATIGA)* and the *ASEAN Comprehensive Investment Agreement (ACIA)*. These instruments lower tariff barriers and strengthen investment protection, providing legal certainty for MSMEs to participate in regional value chains (Chia, 2013; Severino & Menon, 2017). Second, *policy coordination* for MSMEs through the *ASEAN Coordinating Committee on Micro, Small and Medium Enterprises (ACCMSME)* and the *ASEAN SME Policy Index*, which serve as benchmarking tools for policy evaluation and harmonization among member states.

Through these mechanisms, countries can engage in mutual learning and identify domestic policy bottlenecks that hinder MSME competitiveness (OECD, ERIA, & ASEAN, 2018). Third, *connectivity and trade facilitation*, guided by the *Master Plan on ASEAN Connectivity (MPAC)*, which focuses on improving logistics infrastructure, customs efficiency, and product standards harmonization—critical factors for MSMEs to reduce cross-border trade costs (ADB, 2020; Dent, 2008).

ASEAN institutions thus function not only as *rule-making* entities but also as drivers of

capability-building and *compliance facilitation*. Through initiatives such as the *ASEAN SME Academy* and various innovation support programs, ASEAN helps MSMEs enhance managerial, digital, and entrepreneurial skills. Concurrently, through regulatory harmonization and the implementation of *Mutual Recognition Arrangements (MRAs)*, ASEAN assists businesses in meeting regional product and service standards (OECD, ERIA, & ASEAN, 2018; ASEAN Secretariat, 2015). The combination of these two functions is crucial to ensure that economic liberalization leads not only to market openness but also to the readiness of business actors to capitalize on such opportunities effectively.

Nonetheless, the effectiveness of ASEAN's institutional role still faces several limitations. The *ASEAN Way*—a consensus-based and non-binding approach—often results in inconsistent policy implementation among member states (Chia, 2013; Severino & Menon, 2017). Moreover, data asymmetries and differing implementation capacities across countries hinder *outcome-based policy monitoring*. Infrastructure and digital connectivity gaps further reduce the effectiveness of MPAC, particularly for Indonesian MSMEs operating in regions with high logistics costs (ADB, 2020). Additionally, MSME representation in regional policy formulation remains weak, meaning that the voices of small business actors are not yet fully integrated into ASEAN-level decision-making (Dent, 2008).

Therefore, aligning national policies with ASEAN's institutional instruments is critical to ensure that economic liberalization translates into real competitiveness gains for Indonesian MSMEs. Efforts should include accelerating product certification to meet regional standards, expanding export

financing and credit guarantee schemes, strengthening logistics readiness, and enhancing digital technology adoption to broaden cross-border market access. Indonesia must also play a more proactive role in leveraging frameworks such as the *ASEAN SME Policy Index* and *ACCMSME* to ensure that domestic policies align with regional integration priorities.

Critically, ASEAN must also strengthen its institutional performance by shifting from a *commitment-based* to an *outcome-oriented* approach. Success indicators should include concrete measures such as the increase in the number of MSMEs certified under regional standards, growth in cross-border exports by small enterprises, and the reduction of non-tariff barriers affecting MSMEs. ASEAN could consider establishing an *ASEAN MSME Facilitation Window*—a technical assistance and financing mechanism dedicated to supporting MSMEs' first exports. Additionally, implementing peer reviews and publishing scoreboards on non-tariff trade barriers among member states could enhance transparency and exert moral pressure to accelerate policy reforms.

In conclusion, ASEAN's institutional framework has laid an essential foundation through regulatory design, policy coordination, and capacity development—transforming the principles of economic liberalization into inclusive competitiveness. The key challenge ahead lies in ensuring effective implementation at the *MSME interface* level through measurable policies, targeted export financing, accelerated standard recognition, and strengthened logistics and digital infrastructure to sustain regional economic integration in a more inclusive and resilient manner.

VI. INDONESIA'S NEED TO STRENGTHEN MSME COMPETITIVENESS

Indonesia's need to strengthen the competitiveness of its MSMEs in the ASEAN market has become an increasingly urgent strategic issue amid the deepening regional economic integration. Although Indonesia hosts approximately 65 million MSMEs—accounting for more than 93% of all MSMEs in ASEAN—the sector's contribution to national exports remains relatively low, at around 15–16% of total non-oil and gas exports. This condition reflects a gap between the large number of MSMEs and their limited competitiveness at the regional level. The scale advantage has not been matched by production efficiency, product quality, or adaptability to global market standards and dynamics (ASEAN Secretariat, 2015; OECD, ERIA, & ASEAN, 2018).

The structural weaknesses of Indonesian MSMEs lie in low productivity, limited access to export financing, and minimal participation in regional value chains (RVCs). Many MSMEs remain at the upstream stage of production with low value-added activities and lack direct connections to international supplier or buyer networks (ADB, 2020; Dent, 2008). Additional obstacles arise from their limited compliance with international standards such as quality assurance and HACCP/ISO certification, which are prerequisites for entering export markets. The high cost of certification and lengthy bureaucratic procedures often hinder MSMEs from accessing foreign markets (OECD, 2019).

Furthermore, inefficiencies in logistics infrastructure contribute to high domestic and export distribution costs. Uneven interregional connectivity hampers supply reliability and delivery timeliness—critical factors in maintaining the confidence of regional buyers. Institutionally, the lack of regulatory harmonization among ministries and local governments prolongs export

licensing processes and increases business uncertainty (ASEAN Secretariat, 2015).

Efforts to strengthen the competitiveness of Indonesian MSMEs should focus on addressing these structural barriers through *outcome-based competitiveness* strategies. First, the government must accelerate product certification and standardization programs to align with ASEAN's *Mutual Recognition Arrangements (MRAs)*. Second, greater participation in regional value chains can be achieved through *supplier upgrading compacts* that link MSMEs with major buyers in priority sectors such as agro-industry, furniture, and handicrafts. Third, export financing should adopt a transactional model—based on orders or contracts—to ensure timely access to working capital for business actors.

Moreover, cross-border trade digitalization must become a national priority. Through integration with the *ASEAN Single Window*, MSMEs can utilize digital platforms for export documentation, shipment tracking, and cross-border payments, thereby significantly reducing transaction costs and processing times. These initiatives should be supported by robust interagency governance and outcome-oriented performance indicators, such as the number of MSMEs obtaining regional certification, the increase in actual export value, and participation rates in ASEAN supply chains.

Critically, Indonesia's greatest challenge is no longer the quantity of its MSMEs but the quality and competitiveness of their capabilities. Without structural reforms and consistent policy implementation, Indonesia's dominance in MSME numbers could become a burden rather than an advantage. Therefore, strengthening MSME competitiveness means transforming *scale potential* into *competitive scale*—a business scale capable

of generating added value, innovation, and sustainable export competitiveness at both regional and global levels.

Country	Estimated Number of MSMEs*
Indonesia	~ 65.5 million
Thailand	~ 3.2 million
Malaysia	~ 1.2 million
Philippines	~ 1.1 million
Vietnam	~ 700,000
ASEAN region (total)	~ 70 million

*MSMEs includes micro, small, and medium enterprises, though definitions differ by country.

Figure 5. Estimated Number of MSMEs in Selected ASEAN Countries

Based on the table above from the *ADB Asia SME Monitor 2022*, the total number of enterprises in Indonesia—including micro, small, medium, and large businesses—reached approximately 65,471,134 entities. This finding aligns with the results of the *MSMEs Digital Exports in Southeast Asia (2022)* survey conducted by ICC-Google, which reported that Indonesia had around 65,465,497 MSMEs categorized as firms according to the survey's definition. The consistency between these two sources reinforces the general estimate that Indonesia has over 65 million MSMEs, which contribute significantly to the national economy—accounting for about 97% of total employment and 60% of Gross Domestic Product (GDP). These figures demonstrate that the MSME sector serves as the backbone of Indonesia's economy and plays a pivotal role in driving national economic development.

However, for other ASEAN countries such as Malaysia, Thailand, and Vietnam, specific data on the number of MSMEs are not always publicly available in official

publications, such as those issued by the ADB or the ASEAN Secretariat. This indicates a lack of harmonized data across ASEAN member states, which in turn poses a challenge to developing a comprehensive and integrated regional MSME database.

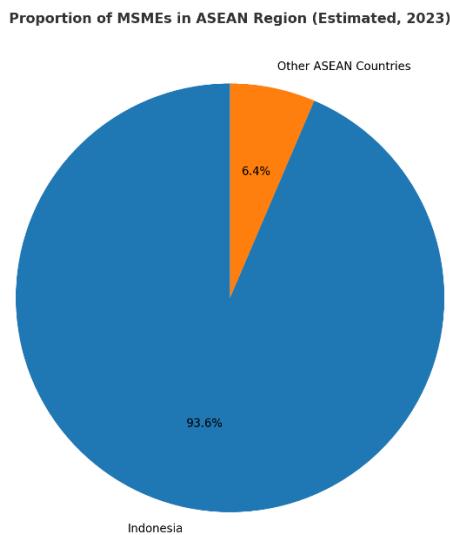


Figure 6. Proportion of MSMEs in ASEAN Region

The pie chart above illustrates the proportion of Micro, Small, and Medium Enterprises (MSMEs) in the ASEAN region based on 2023 estimates. The chart indicates that Indonesia dominates approximately 93.6% of the total MSMEs in ASEAN, while the remaining 6.4% are collectively accounted for by other ASEAN member states. This visualization highlights Indonesia's substantial dominance within the ASEAN MSME landscape.

With around 65.5 million MSMEs, Indonesia represents nearly the entire population of micro, small, and medium enterprises in the region. Meanwhile, approximately 4.5 million MSMEs are distributed across other ASEAN countries, including Thailand, Malaysia, Vietnam, and the Philippines. This dominance underscores Indonesia's crucial role in shaping regional MSME policies, digitalization strategies, and capacity-

building programs within the framework of the ASEAN Economic Community (AEC).

Country	MSME exports (value / share)	Reference year	Main export destinations (top)	Key references
Indonesia	15.7% of non-oil & gas exports (share)	2021	China, United States, Japan, India, Singapore	Kemenkop UKM via IPB note (share) (fem.ipb.ac.id); OEC country profile for destinations (2023) (OEC World)
Malaysia	RM 152.2 billion (12.2% of total exports)	2023	China, Singapore, United States, Hong Kong, Japan	SME Corp Malaysia news (value & share) (SME Corp); OEC (destinations 2023) (OEC World)
Thailand	13.42% of total exports (share)	2019	United States, China, Japan, Australia, Vietnam	World Bank citing OSMEP (share) (World Bank); OEC (destinations 2023) (OEC World)
Philippines	=25% of total export revenues (share)	2021	China, United States, Japan, Hong Kong, Singapore	PhilStar citing DTI (share) (PhilStar); TrendEconomy (destinations 2023) (TrendEconomy)

*Important note: The most consistent and frequently cited figure for Indonesia is the share of MSME exports, approximately 15.7%. Absolute export values in rupiah or U.S. dollars specifically for MSMEs are not regularly published by Statistics Indonesia (BPS). In contrast, Malaysia officially reports a total MSME export value of RM 152.2 billion. Thailand and the Philippines more commonly disclose the percentage contribution of MSMEs to total exports rather than absolute values.

Figure 7. MSME Exports in Selected ASEAN Countries and Main Destinations

Based on the available data, the contribution of Indonesian MSMEs to national exports is estimated at around 15–16% of total exports, with major destinations including China, the United States, Japan, India, and Singapore (Kemenkop UKM; FEM IPB, 2021). Meanwhile, Malaysia recorded MSME export values of RM 152.2 billion in 2023, equivalent to 12.2% of its total national exports, with key markets in China, Singapore, and the United States (SME Corp Malaysia, 2023). In Thailand, MSMEs contributed 13.42% to exports in 2019, with the largest export destinations being the United States, China, and Japan (World Bank, 2019). As for the Philippines, MSMEs accounted for approximately 25% of total exports, primarily targeting China, the United States, and Japan (PhilStar, 2021).

This comparison indicates that MSME contributions to exports across ASEAN countries remain relatively modest compared to total foreign trade, yet they play a vital role in product diversification and local economic strengthening. The

differences among countries can be attributed to variations in MSME definitions—such as the number of employees, turnover, and assets—as well as differences in national statistical reporting methods. Reports from the Asian Development Bank (ADB) and the ASEAN Secretariat also highlight cross-country data limitations, which make direct comparisons not entirely equivalent.

To obtain export value data in a fully comparable currency (e.g., USD, RM, or IDR) across ASEAN countries, further analysis is required by extracting country-specific appendices from the ADB Asia SME Monitor or consulting the latest national statistical reports. This step would strengthen the empirical foundation for comparing MSME export performance at the regional level and help identify potential sectors with the highest export competitiveness in each country.

VII. REGIONAL ECONOMIC INTERDEPENDENCE AND INDONESIA'S ECONOMIC DIPLOMACY

Regional economic interdependence within the ASEAN region has created increasingly close relationships among member states through trade, investment, and cross-border data flows. For Indonesia, this condition offers significant opportunities to expand markets and enhance MSME competitiveness through cross-country learning and participation in regional value chains (RVCs). However, such interdependence also presents new challenges, including increased exposure to external shocks, dependence on specific markets, and complex cross-border regulatory frameworks that may constrain national economic flexibility (Keohane & Nye, 1977; Dent, 2008). In this context, Indonesia's economic diplomacy must evolve from a traditional *market-seeking* approach toward a more proactive *rules-, standards-, and connectivity-shaping*

diplomacy—actively contributing to the formulation of regional norms, standards, and economic infrastructure.

While greater market access through free trade agreements such as the *ASEAN Trade in Goods Agreement (ATIGA)* has benefited Indonesia, the primary barriers now arise from *behind-the-border costs*, including differing standards, customs procedures, and high logistics expenses. Therefore, Indonesia's economic diplomacy should focus on expanding *Mutual Recognition Arrangements (MRAs)* for MSME-related sectors, accelerating the implementation of *single window systems* and cross-border *electronic certification*, as well as harmonizing *sanitary and phytosanitary (SPS)* measures and *technical barriers to trade (TBT)*. These efforts would help small enterprises reduce compliance costs and shorten export processing times (ASEAN Secretariat, 2015; OECD, ERIA, & ASEAN, 2018).

Within the framework of the *Master Plan on ASEAN Connectivity (MPAC)*, connectivity diplomacy also carries strategic importance. Strengthening physical, logistical, and digital linkages among ASEAN countries can lower transaction costs and improve supply chain reliability. Indonesia should leverage this forum to advocate for funding priority logistics corridors, simplifying cross-border procedures for small businesses, and integrating digital trade systems that enhance MSME efficiency (ADB, 2020). Additionally, Indonesia's economic diplomacy can adopt a *minilateral* approach—forming small, sector-based coalitions with countries that share similar interests, such as Thailand and Vietnam—to accelerate agreements on product certification and trade facilitation.

Indonesia's export dependence on major markets such as China, the United States, and Japan underscores the need for export

diversification to prevent systemic economic risks. In this regard, economic diplomacy should emphasize strengthening regional trade finance mechanisms, developing export guarantee schemes for emerging MSMEs, and promoting cooperative efforts to mitigate logistics disruptions that raise export costs and risks. Furthermore, effective economic diplomacy requires strong domestic reforms. The implementation of a *national single window*, simplification of certification procedures, and alignment of central and regional policies will enhance Indonesia's credibility among ASEAN partners and strengthen its bargaining position in regional negotiations (ASEAN Secretariat, 2015).

In conclusion, regional economic interdependence within ASEAN not only creates mutual dependency but also offers a strategic space for Indonesia to expand its economic diplomatic influence. If managed adaptively and proactively, this interdependence can be transformed from a source of vulnerability into a source of competitive advantage. Indonesia's transformation toward *rule-shaping, standard-recognizing, and connectivity-oriented economic diplomacy* will be essential to ensuring the success of Indonesian MSMEs in navigating the increasingly competitive landscape of the ASEAN Economic Community (AEC).

VIII. CONCLUSION

This paper demonstrates that the competitiveness of Indonesian MSMEs in the ASEAN market is determined by their ability to convert massive scale—over 65 million enterprises—into measurable competitive advantage. Within the framework of liberalism and ASEAN economic integration, market openness and regional institutions (AEC, ATIGA, ACIA, ACCMSME, ASEAN SME Policy Index, MPAC) provide opportunities for access, standardization, and cross-border learning.

However, the relatively modest export contribution of Indonesian MSMEs—around 15–16%—reveals a gap between potential and performance, particularly in areas such as compliance with standards (SPS/TBT), productivity and technology adoption, transaction-based export financing, and logistics and connectivity efficiency. Regional economic interdependence amplifies the benefits of cooperation but also heightens exposure to supply chain disruptions and policy spillovers, requiring more proactive economic diplomacy to shape standards, expand certification recognition, and accelerate digital trade facilitation.

The most impactful directions for strengthening competitiveness include:

1. Accelerating certification and standard harmonization recognized by ASEAN through *Mutual Recognition Arrangements (MRAs)* and providing conformity assessment support for priority sectors;
2. Integrating into regional value chains (RVCs) through *supplier upgrading programs* directly aligned with buyer requirements;
3. Implementing transaction-based export financing, including PO/invoice financing, guarantees for first-time exporters, and foreign exchange risk mitigation;
4. Advancing digital cross-border enablement through the *ASEAN Single Window*, e-Certificate of Origin, e-invoicing, and a cross-border e-commerce playbook; and
5. Synchronizing central-local regulations via a domestic single window with clear Service Level Agreements (SLAs) to reduce *time-to-export*.

At the regional level, Indonesia's diplomacy should shift from mere market access toward standards and connectivity diplomacy, building sector-based (minilateral) coalitions and promoting outcome-based metrics, such as the

percentage of MSMEs certified under ASEAN standards, median days-to-export, realized cross-ASEAN contracts, and on-time, in-full (OTIF) delivery performance.

Overall, Indonesia's advantage will no longer be measured by the sheer number of registered MSMEs, but by how many are *ready, recognized, and connected* within the regional trade ecosystem. Anchoring ASEAN instruments to domestically embedded, results-oriented delivery mechanisms will transform interdependence from a source of vulnerability into a source of strength—empowering Indonesian MSMEs to navigate regional competition with inclusive, sustainable, and measurable competitiveness. For future research, more harmonized cross-country data (including MSME definitions and firm-level export indicators) and policy impact evaluations based on experimental approaches (policy pilots) are needed to elevate recommendations from *best practices* to *proven practices*.

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