

THE IMPACTS OF TRADE LIBERALIZATION ON POVERTY REDUCTION IN INDONESIA

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Abstract: Nowadays, trade liberalization is considered as development strategy policy to increase economic growth and reduce poverty in many countries, particularly in developing countries. It is reported that Indonesia has been actively joining many trade agreements in order to ease the distribution of goods and services to other countries. Hence, this study analyses the impact of trade liberalization on poverty reduction by using an Ordinary Least Square (OLS) method from 1984 to 2017. The Trade Openness Ratio (TOR) is used as a dependent variable in order to measure trade liberalization. Other variables such as GDP, exchange rate and labor force are considered as control variables. The empirical result shows that TOR and labor force have a positive impact on poverty, whereas GDP and exchange rate have a negative impact. This finding is different with previous researches, particularly where trade liberalization has been negatively affecting poverty. Such a result is justifiable because Indonesian firms are not ready to compete with foreign firms where high competitiveness exist.

Keywords: Trade Liberalization; Indonesia; GDP; Exchange Rate; Labor Force

JEL Classification: F10, F19, F47

INTRODUCTION

In this globalization era, trade liberalization compromises lots of benefits to many countries, especially for the developing ones. It is reported that the number of exported products, particularly in manufacturing goods, has increased rapidly over the last 30 years (Levin and Ohlin, 2008). Most parts of Asia and Africa continents (Cockburn, Decaluwé, and Robichaud, 2006) experience the gains of trade liberalization, including an increase on welfare society and reduction in poverty level (Hayashikawa, 2009). Ghana (Bhasin and Annim, 2005), Philippines, Nepal, India, Pakistan (Cockburn, Decaluwe, and Robichaud, 2008), and Indonesia (Kis-Katos and Sparrow, 2013) exemplify the countries that experience

the benefit of trade liberalization in these recent decades.

Indonesia joined General Agreement of Tariff and Trade (GATT) since 1950. It was the first agreement that Indonesia was involved. Then, it was followed by many other trade agreements among nations. By joining trade liberalization, Indonesia changes the orientation of trade policy from inward looking to outward looking. Even though Indonesia believes that international trade will improve economic welfare, yet the government should be aware of the consequences of implementing this policy. Hence, by increasing specialization goods by reducing transportation cost, Indonesia can sustain their economic growth for a long-term period (Levin and Ohlin, 2008).

Openness to trade is an important element of economic policy to achieve the sustainability