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Analysis of The Relationship Between Labor Market, Currency Exchange Rate Stability, Product Quality and International Trade Competitiveness

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Abstrak

Tujuan dari penelitian ini adalah untuk mengidentifikasi dan mengukur besarnya dampak persaingan ekonomi terhadap hasil perekonomian. Mikrodata yang digunakan berasal dari data sensus manufaktur tahunan dan data perdagangan. Temuan penelitian menunjukkan bahwa peningkatan volume impor dapat meningkatkan sebaran pekerja di sektor informal, khususnya pekerja yang bekerja di perusahaan kecil. Dampak guncangan kompetisi bisnis terhadap margin penyesuaian jangka pendek juga bervariasi, dimana perusahaan dengan produktivitas awal yang lebih rendah menghadapi biaya penyesuaian yang paling besar. Hal ini menunjukkan pentingnya peningkatan produktivitas untuk bertahan dalam persaingan global.

Kata Kunci: *Persaingan, Ekonomi, Perusahaan, Perdagangan*

Abstract

The aim of this research is to identify and measure the magnitude of the impact of economic competition on economic outcomes. The microdata used comes from annual manufacturing census data and trade data. Research findings show that increasing the volume of imports can increase the distribution of workers in the informal sector, especially workers working in small companies. The impact of business competition shocks on short-run adjustment margins also varies, with firms with lower initial productivity facing the greatest adjustment costs. This shows the importance of increasing productivity to survive in global competition.
Keyword: *Competition, Economic, Firms, Trade*

INTRODUCTION

Economic crises are indeed a phenomenon that often occurs in modern history, and the possibility of facing a crisis is greater in developing countries. The recent international financial crisis has shown that developed countries are also not immune from this crisis. The international macroeconomic literature has made great progress in classifying and understanding most of the causes and consequences of these various crisis episodes (Kusnadi, 2021). In general, the crisis that hit developing countries was characterized by a large contraction in real income, a significant reduction in total factor productivity, a depreciation of the real exchange rate, and a decline in imports. Adjusting the quality of goods is a mechanism that is present in all types of crisis episodes (Rasyid et al., 2023). In simple terms, when real income decreases during a crisis, consumers and producers tend to reduce demand and supply of quality goods. Not only does this quality adjustment mechanism affect welfare, but it also plays a crucial role in comprehending macroeconomic phenomena extensively researched in the literature, like the impact of devaluation on the real economy or the transfer of incomplete devaluation to domestic prices (Arie & Ridlwan, 2023).

Currency crises generally arise from persistent imbalances in a country's balance of payments and current account. The interaction of certain events, both internal and external, can weaken expectations and trigger capital outflows, which then reduce international reserves sharply (Zaena et al., 2023). An exchange rate crisis begins with a real depreciation of the domestic currency, which can cause a breakdown in the payment system, reduce productive investment, negatively impact economic recession, and negatively impact income distribution (Arifin et al., 2023). Depreciation-induced changes in relative loss prices typically serve as the catalyst for balancing external imbalances. The main adjustment variable is usually imports, which can fall sharply due to reduced real consumer incomes and domestic spending due to devaluation (Kusnadi, 2023). Depreciation can also increase the cost of imported inputs and decrease their use, significantly reducing the productivity of domestic firms. This can provide feedback on reductions in real product originating from a recessive economic context (Sudirjo et al., 2024).

The idea that international trade and globalization tend to increase long-term welfare is based on the concept of reallocating productive factors towards industries with comparative advantages and firms with higher productivity (Suharyat et al., 2022). This occurs due to greater access to imported inputs and new export markets by domestic companies, as well as an increase in consumer surplus from a variety of cheaper products (Ibrahim et al., 2024). However, market disruptions often disrupt this reallocation process, making the transition difficult or slow. Furthermore, this reallocation can lead to losses like the depletion of human and physical capital, resulting in an uneven distribution among regions, industries, companies, and workers with diverse characteristics (Tanto, 2023). In many cases, technological advances also have a comparable impact on international trade. Therefore, the study of the impact of globalization and technological change becomes very relevant in understanding the labor market, the potential reallocation of different economies, income distribution, and the general well-being of the population (Sari et al., 2024).

To address the costs of adjustment and realize the long-term benefits of globalization, it is important to pay attention to the speed of the adjustment process. The effectiveness of this reallocation process depends greatly on the productive structure of the economy, the characteristics of the workforce, and the nature of existing institutions (Nurdiani et al., 2024). Parent company diversification, the absorptive capacity of internationally competitive industries and firms, the educational level, age, and job type of the workforce, as well as labor market flexibility, protection networks, and institutional policy responses, all play an important role in this process (Harsono et al., 2024). Intensifying globalization may deepen tensions between workers experiencing negative impacts in the short term and their labor outcomes in the long term and lead policymakers to focus on long-term well-being (Apriliani et al., 2023). Therefore, it is important to study the companies or industries that are most sensitive to competitive shocks in order to gauge the potential impact of globalization on the labor market, as well as analyze possible cost-effective policies that can design adjustment processes or provide compensation to affected workers.

RESEARCH METHOD

The microdata used comes from two main sources. Data comes from the annual manufacturing census. This data encompasses all manufacturing companies with ten or more employees. The main modules of this survey include information regarding company characteristics such as the number of employees, total salary expenditure, purchases of investment goods, intermediate inputs, sales revenue, gross production value, industry affiliation, area of activity, etc. We utilize trade data derived from commodity trade statistics. Then truncated samples along several dimensions to improve data quality and avoid inconsistencies. We removed unaccounted signatures that included complete information on the use of inputs or production values. Then removed firms that were present in one sample year but stopped reporting information in that particular year. We analyzed the data using descriptive statistical methods. This method helps in providing an overview of the data, including the distribution, central tendency, and variation of the observed variables.

RESULT AND DISCUSSION

Exchange rate crises are a frequent phenomenon in modern history. Persistent current account deficits in the balance of payments often trigger these crises. Currency devaluation makes it possible to adjust the trade balance, mainly by reducing the volume of imports. After devaluation, there is an important effect on the composition of the basket of imports. All studied episodes are characterized by a decrease in the price of imported products, a decrease in quality, and an increase in the participation of relatively lower price and quality varieties. The exchange rate crisis affects various aspects of the economy, including economic growth, inflation, and income distribution. Currency devaluation can trigger inflation because import prices increase, while a decrease in the quality of imported products can reduce consumer welfare. In addition, the increased participation of lower-priced and higher-quality varieties may lead to a decrease in the competitiveness of domestic products. In facing the exchange rate crisis, it is important for the government to take appropriate steps to reduce the current account deficit and improve the trade balance. Such measures may include fiscal policy to control spending and monetary policy to maintain currency stability. Apart from that, it is also important to encourage economic diversification so that it is less dependent on imports and increases the competitiveness of domestic products.

We can develop a theoretical explanation for these facts by involving several relevant economic concepts. The government implements currency devaluation as a monetary policy to lower the domestic currency's exchange rate against foreign currency. Economic theory's concept of market balance explains the impact on the domestic economy. When a currency devalues, the lower exchange rate leads to an increase in the price of imported products measured in domestic currency. On the other hand, the price of domestic products exported abroad becomes cheaper for foreign consumers. Thus, devaluation can affect the composition of a country's imports and exports. In the context of monopolistic competition, companies have market power in determining the price of their products because they have products that are unique or different from their competitors. Companies must weigh the trade-off between lowering product prices to maintain competitiveness in international markets and lowering product quality to maintain a decent profit margin when a currency devalues. The effects of this devaluation can be complex because the company must consider various factors, such as production costs, market demand, and its competitive position. In the long term, a successful devaluation can lead to increased competitiveness of domestic products in international markets, but it can also give rise to challenges such as inflation and economic uncertainty. Therefore, the government can use currency devaluation as one of its policy instruments to address a balance of payments deficit. However, the government must carefully calculate the impact to minimize risks and maximize benefits for the domestic economy.

This counterfactual exercise provides a deeper understanding of the mechanisms that adjust the prices of imported goods due to currency devaluation. Adjustments in the quality of imported goods are the main factor that explains most of the decline in import prices. This suggests that imported producers tend to adjust the quality of their products to remain competitive in the domestic market after currency devaluation. Apart from that, the substitution effect also plays an important role in reducing the price of imported goods. This substitution effect occurs when consumers switch from imported goods, whose prices have increased due to devaluation, to other imported goods, which still have relatively stable prices. This shows that consumers have the flexibility to choose more affordable products after a devaluation occurs. Profit margin adjustments also contributed to lower prices for imported goods, although in a smaller proportion. This shows that imported producers are also willing to reduce their profit margins to keep their product prices competitive in the domestic market. Overall, these results indicate that the mechanism for adjusting the prices of imported goods due to currency devaluation involves adjustments to the quality of goods, substitution effects, and adjustments to profit margins. A better understanding of this mechanism can help governments and economic actors make the right decisions regarding currency devaluation policies and their impact on the domestic economy.

Research on the distributional consequences of devaluation price shifts is an important step towards understanding the economic impact of currency devaluation policies. Preliminary results showing a large degree of heterogeneity in increases in household living costs provide an interesting picture of how different societal groups responded to price changes resulting from devaluation. Future studies that would more deeply examine heterogeneity in quality adjustments would provide better insight into how producers and consumers adjust their preferences for imported goods that experience price changes. This will help better understand the mechanisms of price and quality adjustments in response to currency devaluation. Additionally, considering the interaction between trade policy restrictions and economic outcomes will provide a more complete understanding of the factors influencing the effects of currency devaluation. For example, trade policy restrictions in the automotive sector can influence how imported car prices react to devaluation, while the market power of multinational companies can influence their pricing strategies in the face of changing market conditions. Overall, this research has the potential to provide valuable insights into how currency devaluation affects the distribution of the cost of living and quality adjustment strategies of imported goods, as well as how interactions with trade policy affect overall economic outcomes.

Understanding the impact of competitive shocks on the economies of developing countries is an important step in designing effective policies to address the challenges they face. To improve their economic prosperity, developing countries need to develop education and training programs that suit labor market needs, as well as encourage economic diversification to reduce dependence on sectors that are vulnerable to global competitive shocks. Additionally, we need to strengthen our investment in infrastructure that fosters economic growth and generates new jobs. Implementation of appropriate fiscal and monetary policies is also important to maintain economic stability and create a conducive environment for investment and growth. In addition, the development of a more flexible and efficient labor market, as well as the promotion of foreign investment to bring new technology, capital, and skills to the country, can also increase the competitiveness of local industry. By taking these steps, developing countries can strengthen their economies, reduce social inequality, and improve prosperity for all of their societies.

The research results show that the growth in import penetration causes an increase in the level of informality among exposed workers compared to similar workers from less exposed industries. The impact is more significant for individuals working in small companies. For future projects, it will be important to exploit these competitive shocks to further study the employment trajectories of formal workers. Using a newly published administrative document registration database by the Ministry of Labor, Employment, and Social Security, this research can provide a better understanding of the impact of globalization on formal workers in the country. The results of this research will provide valuable insights for policy designers to address emerging problems, such as increasing levels of worker formality, improving worker protection, and strengthening the overall labor market.

CONCLUSION

Exchange rate crises are a frequent phenomenon in modern history, often triggered by ongoing current account deficits. Currency devaluation allows for adjusting the trade balance by reducing the volume of imports. However, devaluation can also trigger inflation and create other economic challenges. In facing the exchange rate crisis, it is important for the government to take appropriate steps, such as wise fiscal and monetary policies, as well as encouraging economic diversification and increasing the competitiveness of domestic products. Research on the distributional effects of devaluation price shifts indicates that a rise in import penetration can heighten the exposure of workers to informality, particularly those in small firms. Future studies need to go more deeply into understanding the labor force trajectories of formal workers by utilizing newly published administrative data. By better understanding the impact of globalization on formal workers, policy designers can address emerging problems more effectively.

The impact of competitive shocks on domestic firms' short-run adjustment margins also varies, with firms with lower initial productivity facing the greatest adjustment costs. This shows the importance of increasing productivity to survive global competition. Understanding the impact of competitive shocks on the economies of developing countries is an important step in designing effective policies. Education and training programs that match labor market needs, economic diversification, investment in infrastructure, sound fiscal and monetary policies, the development of flexible labor markets, and the promotion of foreign investment can help developing countries strengthen their economies and improve the welfare of their people.

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