JURNAL UPI

VOLUME 5, NO. 2, DECEMBER 2022

REVIEW OF ISLAMIC ECONOMICS AND FINANCE

Journal homepage:
https://ejournal.upi.edu/index.php/rief/index

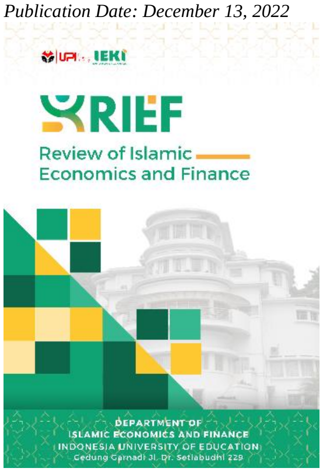
Indonesian Export Diversification to OIC Countries during Covid-19 Pandemic: A Literature Review

Nanda Lismatiara Zubaid*
Universitas Airlangga, Surabaya, Indonesia

Article Info

Paper Type:
Literature Review.

Received: July 23, 2022
Revised: August 25, 2022
Accepted: October 2, 2022
First Available online: November 15, 2022
Publication Date: December 13, 2022



Cite this document

Zubaid, N. L., (2022). Indonesian Export Diversification to OIC Countries during Covid-19 Pandemic: A Literature Review. *Review of Islamic Economics and Finance*, *5*(2), pp. 161-170.

Abstract

Purpose *– The COVID-19 pandemic has had a negative impact on the economies of OIC member countries. The global trading system has been a source of flexibility, diversification, and strength during the pandemic. Export diversification is considered a significant tool to accelerate the pace of economic growth. This study aims to analyze the diversification of Indonesia's exports to the OIC countries during and post-COVID-19.*

Methodology *- To develop export diversification, Indonesia is accelerating several strategies to take advantage of its relationship with OIC countries, including increasing exports of halal products, strengthening market access for Indonesian halal products in foreign markets, and preparing various programs to strengthen business players in exporting halal products.*

Findings *- Post-COVID-19 pandemic recovery, Indonesia's trade balance performance with the OIC countries showed a positive performance by recording a surplus in 2021. Even though during the pandemic in 2019 and 2020, exports to the OIC countries experienced a decline.*

Keywords: Export Diversification, OIC Countries, Covid-19 Pandemic.

*Corresponding author: nanda.lismatiara.zubaid-2021@feb.unair.ac.id

1. INTRODUCTION

Various efforts made to contain the COVID-19 pandemic resulted in a slowdown in global economic growth to 2.8% in 2019 (https://www.sesric.org/publications-detail.php?id=531). Additional fiscal support, anticipated acceleration and expansion of vaccination coverage, and continued adaptation of all sectors of the economy to pandemic life are expected to contribute to the recovery process (IMF, 2021). However, there are growing concerns over uneven recovery and differences between countries.

COVID-19 pandemic has a negative impact on the economies of OIC member countries. With current prices, the total GDP of OIC member countries contracted by 5.6% from US$ 7.3 trillion in 2019 to US$ 6.9 trillion in 2020 (See: https://www.imf.org/en/Topics/imf-and-covid19/Fiscal-Policies-Database-in-Response-to-COVID-19). As can be seen in figure 1, most of the total GDP of OIC countries is still produced by several member countries, which reflects the large difference in the size of the economy. In 2020, the five largest OIC countries accounted for more than half (51.6%) of total GDP, while this share reached 75.6% for the ten largest countries. Indonesia with a GDP exceeding US$1 trillion, has the highest share in OIC GDP (15.4%), followed by Turkey (10.5%), Saudi Arabia (10.2%), Iran (9.3%), and Nigerian (6.3%).

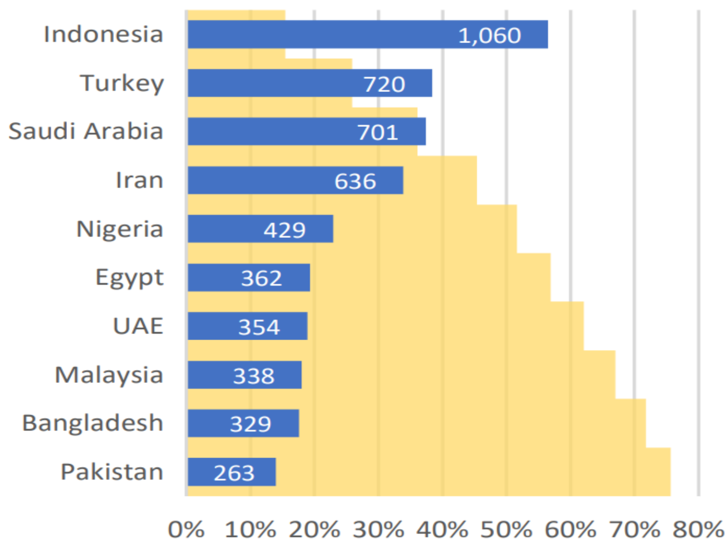


Figure 1. Top 10 OIC Countries by GDP for 2020 (In US$, billion)
Source: (See: https://www.imf.org/en/Publications/SPROLLs/world-economic-outlook-databases)

The COVID-19 pandemic also has a negative impact on the figure economies of OIC member countries, such as most of the world's economies. With current prices, the total GDP of OIC member countries contracted by 5.6% from US$ 7.3 trillion in 2019 to US$ 6.9 trillion in 2020 As can be seen in figure 1, most of the total GDP of OIC countries is still produced by several member countries, which reflects the large difference in the size of the economy. In 2020, the five largest OIC countries accounted for more than half (51.6%) of total GDP, while this share reached 75.6% for the ten largest countries. Indonesia with a GDP exceeding US$1 trillion, has the highest share in OIC GDP (15.4%), followed by Turkey (10.5%), Saudi Arabia (10.2%), Iran (9.3%), and Nigerian (6.3%).

Exports play an important role in driving economic growth. According to Novita & Herianingrum (2020), exports reflect trade activities between countries that can provide impetus for the dynamics of international trade growth, so that a developing country has the opportunity to achieve economic progress commensurate with more developed countries. International trade is contributing to accelerated economic recovery from the COVID-19 pandemic crisis for many developing and least developed countries, which have limited ability to spur economic recovery through fiscal stimulus packages (See:https://www.wto.org/english/res_e/publications_e/wtr21_e.htm). This is due to the continued demand for foreign goods on the export side. Increasing the efficiency of domestic services that affect trade also plays an important role in building and supporting economic resilience. Global trade is more resilient during the COVID-19 pandemic than it was during the 2008-2009 global financial crisis (Notteboom, 2021). This means the global trading system has become a source of flexibility, diversification and strength during the pandemic, helping countries cope by facilitating access to critical medical supplies, food and consumer goods, and by supporting economic recovery. Following grafik in figure 2:

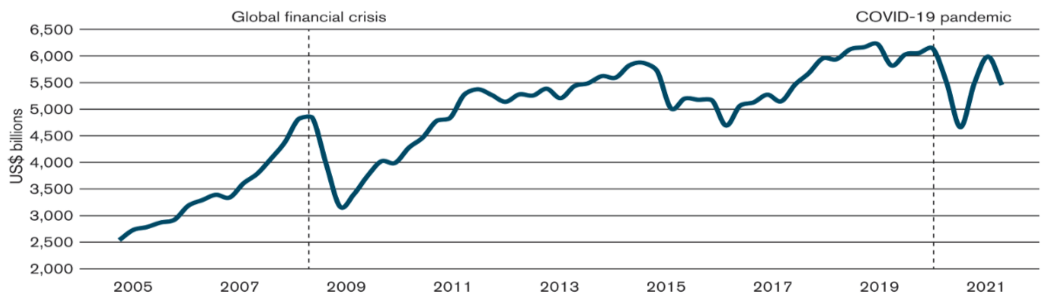


Figure 2. Global Trade

Source: (See: https://www.wto.org/english/news_e/archive_e/stat_arc_e.htm)

Under the unprecedented impact of the pandemic, global trade volume is expected to have decreased by 8.5% in 2020 as seen in the image above. World trade volume increased by 8.4% in 2021. Global trade growth in 2021 was supported by a broad recovery in global activity, with contributions from the easing of restrictions imposed on the pandemic along with rapid and widespread vaccination (See: https://www.imf.org/en/Topics/imf-and-covid19/Fiscal-Policies-Database-in-Response-to-COVID-19).

Exports are important in low- and middle-income countries to provide macroeconomic stability (Gözgör, 2017). However, the lack of export diversification policies, the average return on exports, and the stability of the casual relationship between exports and growth lead to instability in the export-growth relationship (Furuoka, 2019).

The phenomenon of export diversification is considered a significant tool to accelerate the pace of economic growth in developing countries. However, trade restrictions to secure national supply often lead to trade retaliation from other countries, so policies for trade diversification are more likely to build and support economic resilience which will ultimately reduce macroeconomic volatility. So that the diversification of production and export markets is very important to maintain market share (Khan, 2021).

2. LITERATURE REVIEW

Export diversification, defined as the breadth of the composition of an economy's export basket, is a means to accelerate economic growth, reduce volatility due to price, demand and exchange rate fluctuations, and stabilize export earnings in the long term (Bajaj et al., 2022).. In addition, export diversification allows the government to achieve several of its macroeconomic objectives, namely sustainable economic growth, a satisfactory balance of payments situation, employment and income redistribution (Sannassee et al., 2014).

Exports are divided into two categories: product and geography. Product diversification is carried out by changing or expanding the existing basket of export commodities. Meanwhile, geographical diversification is the expansion of the set of markets entered (Arranguez & Hinlo, 2019). Some conditions if a country's exports are concentrated in several products, the country is more vulnerable to a decrease in demand for a single product which in turn increases aggregate volatility. On the other hand, if exports are concentrated in a few export destinations, a destination-specific demand shock, such as a recession, can have a major impact on export earnings. Diversification of export products and diversification of export markets can affect imports and exports so that they have an impact on the trade balance and economic growth (Akbas, 2021).

Export dependency on a particular country is extremely risky if it has not been anticipated by expansion into new markets, hence export diversification is essential, particularly in promising countries that are expanding infrastructure, logistics, and transportation capabilities (Prasetya & Oktaviani, 2017). Horizontal diversification has the potential to increase a country's export earnings while increasing income stability against shocks and fluctuations. By adding new products and/or sectors to existing products and/or sectors, countries can reduce their reliance on a number of commodity goods that are mostly vulnerable to price increases and decreases (Karahan, 2017). In terms of fluctuations, Karahan explained that vertical diversification is however assumed to strengthen a more consistent trend of economic growth because price variations in manufactured goods are less than those in basic commodities.

Since December 2019, world trade has suffered greatly from the negative impact of Covid-19 which has deregulated all supply chains of manufactured products, and hampered the commercial strategies of not only countries, but also regional economic development plans within the framework of national integration (See: https://www.sesric.org/publications-detail.php?id=531). The COVID-19 outbreak has had huge economic and financial consequences. The report shows that, in 2020, most macroeconomic indicators deteriorated significantly worldwide, and the OIC member countries were no exception. The OIC countries are not only affected by the outbreak of the domestic pandemic and its consequences, but also from the economic spillover from the deep recession in developed countries (See: https://www.imf.org/en/Topics/imf-and-covid19/Fiscal-Policies-Database-in-Response-to-COVID-19). Countries with persistent trade balance deficits have a negative balanc of payments in the absence of appealing investment opportunities for foreigners, and these countries must face the consequences in the form of foreign loans and grants (Hanif, 2021).

3. METHODOLOGY

This study employs a qualitative method with a literature review approach. This study examines international trade and government policy in responding to a pandemic in Indonesia, using exports to OIC countries as research samples. To supplement current data findings, data from the World Trade Organization, International Monetary Fund, Kemendag, SESRIC, and Trade Map were used.

4. RESULTS AND DISCUSSION

The COVID-19 crisis and financial shocks highlight the need to have sufficient international reserve buffers in place to help maintain macroeconomic and financial stability in the face of such shocks. Given the differences in the availability of reserves between countries, shocks are not evenly distributed across countries and they do not enter crises in the same way. The rapid spread of COVID-19 and the steps taken by governments to contain it have serious consequences for global trade. Many productive activities have been halted, global value chains have been disrupted, and there have been widespread border closures causing distortions in global supply networks and a decline in demand for goods and services. While global value chains are the main channel for transmitting the impact of COVID-19 to global trade in goods, restrictions on cross-border movement are the main driver of contraction in global trade in services.

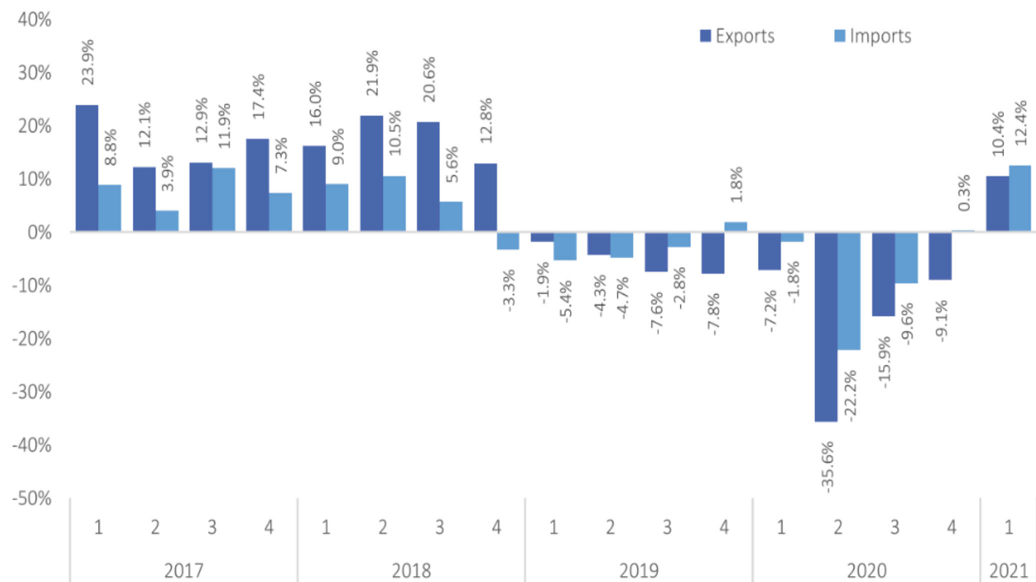


Figure 3. Total Exports and Imports of Goods by OIC Countries
Source: (See: https://data.imf.org/?SK=9D6028D4-F14A-464C-A2F2-59B2CD424B85)

The figure 3 above provides an assessment of the development of trade flows of the OIC countries. With the outbreak of the COVID-19 pandemic, the decline in exports reached up to 35.6% in the second quarter of 2020. After declining for eight consecutive quarters, the total value of exports from the OIC countries again increased during the first quarter of 2021.

4.1. Indonesian Exports

Figure for figure 4 above grafik comparison of Indonesia's exports to the World and the OIC:

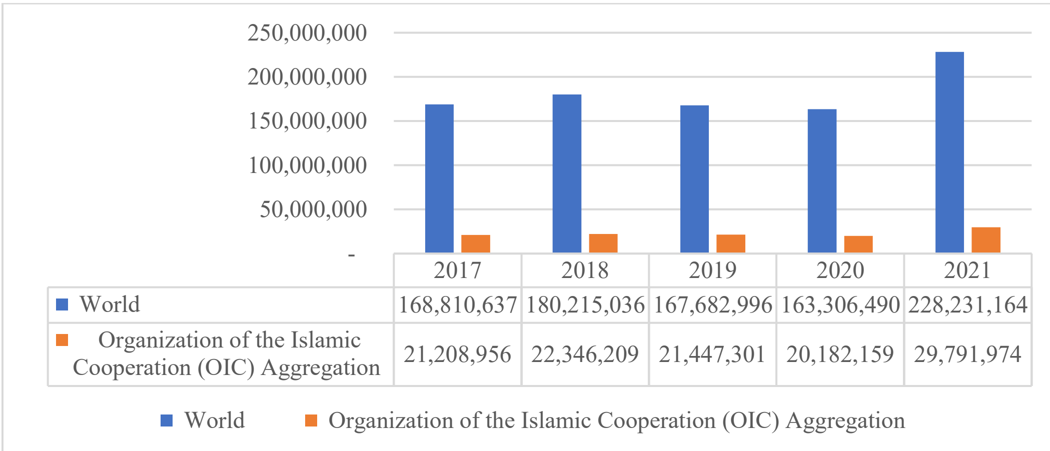


Figure 4. Comparison of Indonesia's Exports to the World and the OIC
Source: (See: https://www.trademap.org/)

Indonesia's export value e fluctuates every year, reaching countries across the world, including OIC members, regardless there is a significant increase in 2021. The graph above shows that Indonesia's overall exports to OIC nations remain low when compared to exports to the rest of the world. The value of Indonesia's exports to OIC members will increase by 47% in 2021 compared to the previous year. The majority of OIC member countries with a Muslim majority have high levels of compliance with certified halal products. As a result, the OIC countries represent a market with numerous potential.

Indonesian exports targeting the international trade market by supplying halal commodities (Rangkuty, 2019). The bigger an OIC member country's trade openness index compared to Indonesia, the more open it is to international trade and the greater the opportunity for Indonesia to export (Azizah & Beik, 2017). Yogatama & Hastiadi (2016) highlighted that democratization and good governance quality (corruption control, government effectiveness, political stability, rule of law, accountability) in Indonesia played a positive and significant role in increasing Indonesia's exports to OIC countries.

4.1. Diversification of Indonesian Exports to the Organization of Islamic Cooperation (OIC)

Export diversification attempts to expand the trade portfolio of both products/sectors and trading partners, contribute to growth, and act as a buffer against crises and economic shocks (Karahan, 2017). Diversification helps countries to hedge against adverse trade shocks by stabilizing export earnings. Diversifying commodities (products) and export structures will increase export income towards higher economic growth (Khan, 2021).Thus, through export diversification, an economy can develop towards the production and export of products that can make a major contribution to economic development.

In terms of how prepared its national ecology is to facilitate the growth of export diversification, Indonesia currently lags behind (Callen, 2014). In order to establish a sharia economy in the OIC nations, Indonesia strives to improve export diversification by taking into account four factors: financial, regulatory, social, and halal food awareness.

Indonesia as a country with the largest Muslim population in the world has not been able to play an optimal role in meeting the demands. In the 2018/2019 Global Islamic Economy Index, Indonesia is ranked 10th in the world as a producer of halal products. Although Indonesia's export performance in Muslim fashion products, halal food, and halal tourism continues to increase from year to year, in aggregate Indonesia has a large net import of halal products and services which results in a deficit in the current account (See: https://www.dinarstandard.com/post/state-of-the-global-islamic-economy-report-2020-2021). Following map in figure 5:

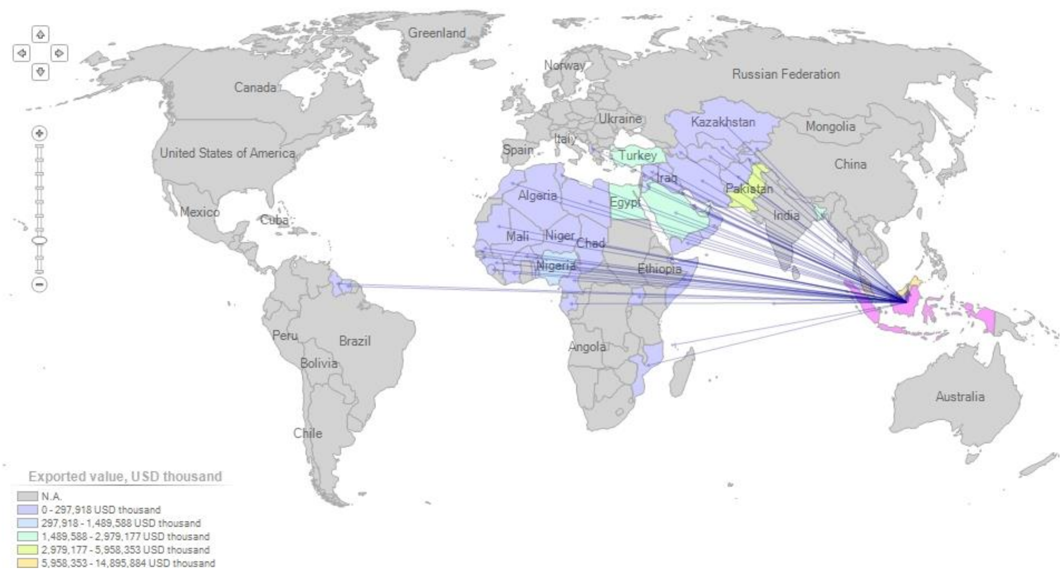


Figure 5. OIC countries exported by Indonesia in 2021
Source: (See: https://www.trademap.org/)

The OIC countries are a very large market consisting of 57 member countries, with a total Muslim population of 1.86 billion people or about 24.1 percent of the total world population. This number does not include Muslims outside the OIC member countries, such as India with 195 million Muslims and Ethiopia with 35.6 million Muslims. OIC countries, as the largest Muslim-majority group, may have the highest potential to become market epicenters. Therefore, on December 13, the Indonesian government issued regulation no. 78/2019 which offers tax incentives for business actors and its expansion to 183 sectors from 145 sectors.

To develop export diversification, Indonesia is accelerating its strategy to capitalize on its relationship with the Muslim world by increasing trade amid pressure from US-China trade tensions (See: https://asia.nikkei.com/Economy/Indonesia-doubles-trade-missions-to-Muslim-markets-in-export-push). This can be seen after the pandemic recovery, the performance of Indonesia's trade balance with the OIC countries showed a positive performance by recording a surplus in 2021. Even though during the pandemic in 2019 and 2020 there was a decline in exports to the OIC countries. Following grafik in figure 6:

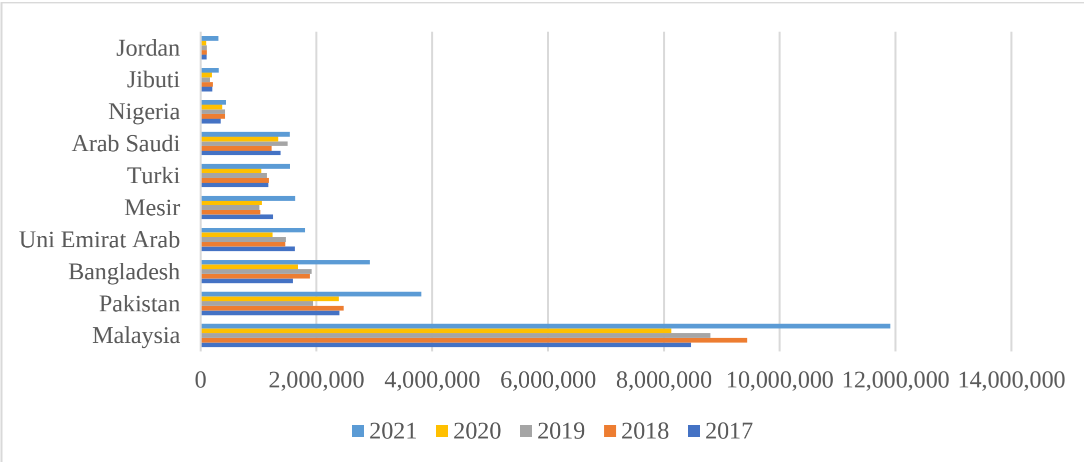


Figure 6. Indonesia's Largest Exports to 10 OIC Countries (in Thousands of US Dollars)
Source: (See: https://www.trademap.org/)

The Indonesian Ministry of Trade (Kemendag) conducted various trade negotiations, including negotiations involving Muslim and non-OIC member countries which are potential markets for Indonesian halal products. OIC member countries that have trade agreements with Indonesia are Pakistan, Mozambique, Palestine, as well as Malaysia and Brunei Darussalam within the ASEAN framework. In addition, Indonesia is currently in the process of negotiating and exploring trade cooperation with other OIC member countries, such as Turkey, Tunisia, Bangladesh, Iran, Morocco, Gulf countries, and several Eurasian countries (See: https://www.kemendag.go.id/storage/article_uploads/vwNnTnjqPFSparAXUya1oRGEMuiB5hFlhPFLW2XZ.pdf).

The COVID-19 pandemic has placed significant downward pressure on trade flows on both the world and the OIC countries, which were already facing increasing challenges prior to the pandemic as a result of trade tensions between major economies. Major international organizations forecast a dramatic decline in global trade. Major international organizations forecast a dramatic decline in global trade (Mishra, 2020)

In 2020, since the increase in COVID-19 cases worldwide, Indonesia was also affected by a decline in exports. Some of Indonesia's exports that have declined to OIC countries include Malaysia, Bangladesh, the United Arab Emirates, and others. After the pandemic, the World Trade Organization (See: https://www.wto.org/english/res_e/publications_e/wtr21_e.htm) projects that global trade will indeed decline in line with initial predictions, but that further recovery will strengthen as a result of increasing demand for consumer goods. Slowly, Indonesia's exports will also increase in 2021, marked by increased exports in 42 OIC countries.

5. CONCLUSION

Diversifying access to global goods and services enables a country to cope with shocks by changing suppliers when a crisis disrupts existing supply relationships, both domestic and foreign. Export diversification is a change in the composition of the product mix or export destinations in a country. Diversification of the export market can affect both imports and exports so that it has an impact on the trade balance and economic growth.

Realizing the potential for export diversification, the Ministry of Trade and Bappenas have several strategies to increase exports to countries of the Organization of Islamic Cooperation (OIC). This strategy combines the various available instruments. First, by utilizing policy instruments, such as the export-import relaxation policy for halal products for export purposes. Second, by strengthening market access for Indonesian halal products in foreign markets. Third, by preparing various programs to strengthen business players in the export of halal products.

REFERENCES

Akbas, Y. E. (2021). The impact of export dynamics on trade balance in emerging and developed countries: An evaluation with middle income trap perspective. *International Review of Economics and Finance*, *76*, 357–375. https://doi.org/10.1016/j.iref.2021.06.014

Arranguez, G. I. S., & Hinlo, J. E. (2019, April). Export geographical diversification and economic growth among ASEAN countries (MPRA paper No. 81333). https://mpra.ub.uni-muenchen.de/81333/1/MPRA_paper_81333.pdf

Azizah, N., & Beik, I. S. (2017). Forecast and determinants of Indonesia's export to the OIC member countries. In A. E. S. Ali, A. G. Ismail, R. M. Yusof, & N. H. Ahmad (eds.), *Intra trade in OIC*. Islamic Development Bank.

Bajaj, P., Baris, K., Gonzales, P., Jabagat, C. R., Lazatin, J. E., & Tan, E. (2022, March). A case for value-added exports in the estimation of export diversification in Asia and the Pacific (ADB Economics Working Paper Series No. 650). https://www.adb.org/sites/default/files/publication/778261/ewp-650-value-added-exports-estimation-export-diversification.pdf

Callen, M. T., Cherif, R., Hasanov, F., Hegazy, M. A., & Khandelwal, P. (2014). *Economic diversification in the GCC: Past, present, and future*. International Monetary Fund.

Furuoka, F. (2019). Export diversification, mean-reversion of exports, and stability of export–growth causality. *International Trade Journal*, *33*(3), 221–238. https://doi.org/10.1080/08853908.2018.1555497

Gözgör, G. (2017). Causal linkages among the product diversification of exports, economic globalization and economic growth. *Review of Development Economics*, *21*(3), 888–908. https://doi.org/10.1111/rode.12301

Hanif, M. (2021). Intra OIC-region trade: Application of gravity model. *Journal of Islamic Business and Management (JIBM)*, *11*(02), 250–266. https://doi.org/10.26501/jibm/2021.1102-002

International Monetary Fund. (2021). *World Economic Outlook, October 2021: Recovery During a Pandemic*. International Monetary Fund.

Karahan, H. (2017). Export diversification in emerging economies. In Ü. Hacioğlu & H. Dinçer (eds.), *Global financial crisis and its ramifications on capital markets: Opportunities and threats in volatile economic conditions* (pp. 287-296). Springer. https://doi.org/10.1007/978-3-319-47021-4_21

Khan, Z. (2021). The roles of export diversification and composite country risks in carbon emissions abatement: Evidence from the signatories of the regional comprehensive economic partnership agreement. *Applied Economics*, *53*(41), 4769–4787. https://doi.org/10.1080/00036846.2021.1907289

Mishra, M. K. (2020). The World after COVID-19 and its impact on Global Economy.

Notteboom, T., Pallis, T., & Rodrigue, J. P. (2021). Disruptions and resilience in global container shipping and ports: the COVID-19 pandemic versus the 2008–2009 financial crisis. *Maritime Economics & Logistics*, *23*, 179-210.

Novita, & Herianingrum, S. (2020). Pengaruh GDP, ekspor dan investasi terhadap inflasi di lima negara anggota IDB. *Jurnal Ekonomi*, *25*(1), 81. https://doi.org/10.24912/je.v25i1.628

Prasetya, D., & Oktaviani, R. (2017). Export performance analysis of Indonesia's main commodity to Middle East in the period of 2010-2014. *The Proceeding of The 1st International Conference and Call for Paper on Trade*.

Rangkuty, D. M. (2019). Indonesia's halal commodity supply for international trade market. *International Halal Conference & Exhibition*, *1*(1), 133–138.

Sannassee, R. V., Seetanah, B., & Lamport, M. J. (2014). Export diversification and economic growth: The case of Mauritius. In M. Jansen, M.S. Jallab & M. Smeets (eds.), *Connecting to global markets: Challenges and opportunities* (pp. 11-23). World Trade Organization.

Yogatama, A. R., & Hastiadi, F. F. (2016). The role of democracy and governance in the enhancement of Indonesian exports to the Organization of the Islamic Cooperation (OIC) countries. *Journal of Economic Cooperation and Development*, *37*(4), 51–78.