DRIVERS OF COUNTRY'S EXPORT PERFORMANCE

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DRIVERS OF COUNTRY'S EXPORT PERFORMANCE

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Abstract

With the imminent execution of the ASEAN free trade era, Indonesia is becoming increasingly exposed to the phenomenon of globalization. Nevertheless, this situation can also provide benefits for Indonesia, one of which by increasing domestic productivity in order to increase exports. It has been well established that exporting is a key channel to achieve a higher level of productivity. The number of research investigating the association between firm-level characteristics and firm's export performance has been numerous. Hence, this study investigates country-level characteristics that will affect its export performance. There are several country-specific macroeconomic dimensions that can differentiate a country from other countries in terms of export performance. Among those factors are: trade openness, real effective exchange rate, FDI inflows, and inflation. Using macroeconomic data from 88 exporter countries, this study tries to seek confirmation whether those factors would influence country's export performance. Managerial implications and suggestions for future research will then be delivered.

Keywords: globalization, macroeconomic characteristics, exporter, export performance

1.RESEARCH BACKGROUND

It has been well established that exporting is a key channel to achieve a higher level of productivity (Yang &Mallick, 2014, Bernard et al., 2003, Helpman et al., 2004; Melitz, 2003). The number of research investigating the association between firm-level characteristics and firm's export performance has been numerous. Eventually, the sum of all firms' export performance and the country's export performance will establish country's export performance itself. When a country involves in a trade, financial transactions among business or consumers from other country will occur. Products and services are exported and imported, investments are made, cash payments are made and cash receipts are received (Graham &Cateora, 2011).In relation with that matter, government plays an important role as export activity heavily depends on domestic economic policy which in turn will affect macro condition within a country, e.g. inflation or Foreign Direct

Investment (FDI) inflows. Hence, this study investigates country-level characteristics that will affect its export performance.

Some countries are blessed with natural resources which allow them to become a successful exporter of particular natural resources such as Saudi Arabia with the oil, Malaysia with the rubber, Indonesia with the coffee; some countries develop sophisticated technology that enable them to become more efficient producers such as South Korea, Japan, or Germany; and some countries are excellent in providing services to consumers around the world such as USA. But, overall their export performance vary. Germany was the top of exporter country in 2013, but China took its position in 2014 (The World Factbook, 2014). Several factors are responsible for this to happen.Yang &Mallick (2014) argued that there are several country-specific macroeconomic dimensions that differentiate a country from others in terms of export performance. Among those factors are: trade openness, real effective exchange rate, FDI inflows, and inflation.

Trade opennes is a contemporary effort to make it easy to exchange goods and services, capital labor, information, and ideas across the borders. It aims to integrate economies and societies at global level (Shahbaz, 2012).Guerrieri&Caffarelli (2012) found that the higher the level of international openness the better the export performance of a country.

Real effective exchange rate (REER) measures the development of the real value of a country's currency against thae basket of trading partners of the country. It is used for many purposes, one of which is assesing the change in price or cost competitiveness (Darvas, 2012). Exchange rate is an important variable of macro economy and has significant influence on interantional trade, directly affects a country on the international market commodity prices, and ultimately affect the country's international competitiveness of commodities (Shen, 2012). Hence, an effort to increase export performance will affected by REER.

Foreign Direct Investment (FDI) plays an important role in developing international trade. FDI is establishment of a business operation in a country by a foreign corporation through setting up a new wholly-owned affiliate, or acquiring a local company, or forming a joint venture in the host economy (Salim, Razavi, & Afshari-Mofradd, 2015).The FDI literature distinguishes four main motives of FDI – natural resource seeking, efficiency seeking, market seeking, and strategic asset seeking (Buckley et al., 2007; Cui, Meyer, & Hu, 2014; Makino et al., 2002). Natural resource seeking aims to secure a firm's supply of resource inputs either for its own production or for sales to business partners outside the host country (Ramasamy, Yeung, &Laforet, 2012). While natural resource seeking FDI may enhance a firm's supply reliability and thus protect its current competitive position, it does not normally improve the firm's ability to utilize and add value to the resources, which is the key factor differentiating a market leader from the followers. Market seeking FDI aims to strengthen a firm's market presence in existing or new foreign markets.Anyhow, FDI eventually will increase domestic productivity and support export performance. While FDI could affect country's export performance, a study by Liargovas and Skandalis (2012) found that FDI decisions depend on country's openness.Zhang and Daly (2011) reveal that China's FDI are flowing to open economic regimes. Al Nasser (2007) and Torrisi et al. (2008) find similar results and conclude that the openness of an economy enhances FDI.

Inflation is the general increase in prices of goods and services which are basic needs for the community or the decline in purchasing power of the country's currency (Statistics Indonesia, 2015). A study by Gylfason (1997) found that high inflation over the last ten years has tended to be associated with low export ... in a large group of countries at all income levels. Inflation affects export because domestic inflation stimulates import spending, given that imports appear relatively cheaper, and dampens export sales, as exports appear more expensive abroad (Economics Online, 2015).

In short, in this era of globalization, it is important for any country to realize that policies that government set will actually affect the performance of domestic and foreign firms operating in their country as well as performance of the country itself, in this case is export performance. Export is important activity, for both firms and economy, since export will generate revenue and profit for firms and also for government which will affect the balance of payment. Since government policies will affect macro economy condition, this study investigates the role of some macro charateristics in the relation with export performance of a country.

2. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

2.1 Export

Exporting accounts for some 10 percent of global economic activity. Exporting can be either direct or indirect. With direct exporting, a company sells to a customer in another country. This method is the most common approach employed by companies taking their first international step because the risks of financial loss can be minimized. In contrast, indirect exporting usually means the company sells to a buyer (importer or distributor) in the home country, which in turn exports the product.Early motives for exporting often are to skim the cream from the market or gain business to absorb overhead. Early involvement may also be opportunistic and come in the form of an inquiry from a foreign customer or initiatives from an importer in the foreign market. Exporting is also a common approach for mature international companies with strong marketing and relational capabilities (Graham &Cateora, 2011).

2.2 Trade Openness and FDI Inflows

Most of studies find that trade openness is positively related to FDI in host country, in particular for export-oriented MNC's that prefer to locate to a more open economy because trade protection generally states higher transaction cost associated with exporting (Jadhav, 2012) and economically conducive environment is likely to be a magnet for foreign business, leading to FDI inflows (Kumar, 2002 in Liargovas& Skandalis, 2012).On the other hand, market-seeking investments can be motivated by the need to overcome external trade barriers, hence FDI is expected to be positively affected by trade openness (Anyanwu, 2012). Hence, ***H1: Trade openness affect FDI inflows***

2.3REER and Export Performance

Real effective exchange rate (REER) can affect aggregate export (Yang &Mallick, 2014). REER as a measure of relative prices can be a key indicator of export competitiveness. REER is employed to control for changes in relative price that are common to all plants, and devaluations may increase the probability of becoming an exporter (Clerides et al., 1998). REER influences the flow of international trade, in the sense that REER as a relative price variable captures the degree of export competitiveness of each country (Yang &Mallick, 2014). Hence, ***H2: REER affect export performance***

2.4FDI Inflows and Export Performance

It is argued that foreign direct investment (FDI) promotes exports of the host countries by increasing the productivity and productive capacity of the host country by increasing capital stock, transfer of technology, managerial skills and upgrading the skills of the local workforce through training. Further, FDI also increases the opportunity for the host countries to export by facilitating access to the new and large foreign markets (Sultan, 2013).

The export of a country is directly affected by FDI in several ways: (a) Exports through processing and assembling (Zhang and Markusen, 1999); (b) Exports through converting import-substituting industries; (c) Exports of new labor-intensive final products(Zhang, 2005); (d) Exports of locally processed raw materials (Zhang, 2005). FDI also enhances the host country's manufacturing exports through spillover effects on local firms' exporting activities (Zhang (2005), specifically by (a) Learning and imitating of domestic firms from foreign firms; (b) Instilling competition and efficiency; (c) Linkage between foreign and local firms. Hence, ***H3: FDI affects export performance***

2.6 Inflation and Export Performance

Inflation is another factor that can affect exporters' performance through its impact on input and output prices. Inflation absorbs the effect of any rise in production costs that can differentiate the performance effect of exporting countries (Yang &Mallick, 2014).Gylfason (1997) finds that high level over the last ten years has tended to be associated with low export. Gylfason (1997) further argued that three possible sources are: (i) inflation-induced overvaluation of national currencies in real terms; (ii) inflation-induced production distortions driving a wedge between the returns to real and financial capital; (iii) the potentially deleterious effects of inflation on saving and investment. Hence, ***H4: Inflation affects export performance***

3. RESEARCH METHOD

3.1 Data and Analysis Technique

Data used are secondary. Trade openness is measured by total import divided by GDP (Squalli& Wilson, 2006). Export performance is measured using export growth.Real effective exchange rate, inflation, and export growth data are retrieved from various resources. While list of top exporter countries is retrieved from The World Factbook. All data are for the year 2014.

Regression analysis is used to analyze relationship among research variables as the purpose of this analysis is to predict changes in dependent variable cause by changes in independent variable(s) (Hair, et al., 2006). The model equationsare as follows:

$$ForeignDirectInvevstmentInflow = a + b_1TradeOpenness \quad \text{... (1)}$$

$$ExportGrowth = a + b_1RealEffectiveExchange\ Rate + b_2ForeignDirectInvevstmentInflow + b_3Inflation \quad \text{... (2)}$$

3.2 Research Model

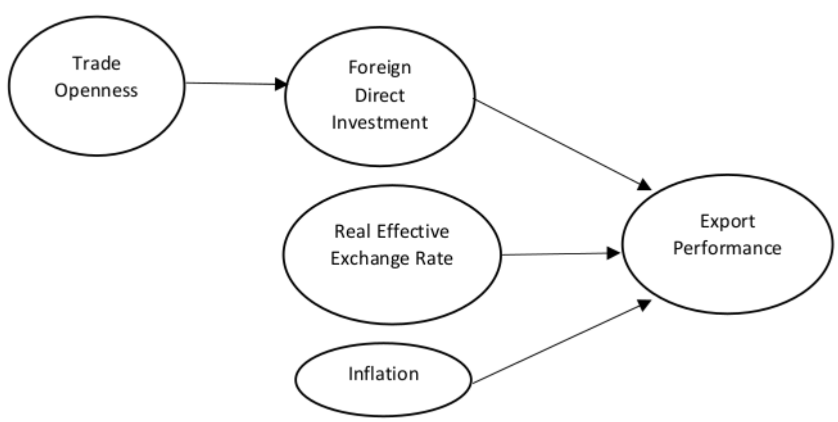

Figure 1
Research Model

4. RESULTS AND DISCUSSION

Using Eviews 7, we used simultaneous equation to test the effects of macroeconomics indicator on export performance. As Table 1 shows, trade openness ($b=391.96$, $p<0.05$) has a positive and significant effect on foreign direct investment inflow. These results support H1. The effect of foreign direct investment (($b=1.694$, $p<0.05$), real effective exchange rate ($b=0.016$, $p<0.05$), and inflation ($b=-0.175$, $p<0.05$) have a positive and significant effect on export performance.Thus, H2, H3, H4are supported.

Table 1 Result of Simultaneous Equation

Independent Variables	Coefficient	Prob.
Dependent Variable: Foreign Direct Investment		
Trade Openness	391.9645	0.0084
Dependent Variable: Export Performance		
Foreign Direct Investment	1.694505	0.0080
Real Effective Exchange Rate	-0.015694	0.0087
Inflation	-0.175097	0.0475

FDI has always been considered as one of drivers of economic growth of a country. it is said to accelerate economic growth through increasing export since FDI will bring technology, managerial skill, and access to international markets. For Indonesia context, government should optimize domestic infrastructure and policies to attract more FDIs.Liargovas& Skandalis (2012) found that trade openness significantly affect the attraction of FDI. They also found that despite this significance, in developing economies, it attract only small amounts of the world FDI. It is because apart from openness, they found that there are some other factors such as political stability, exchange rate stability, and market size positively influence the existence of FDI.

Based on regression analysis outputs we can conclude that real effective exchange rate has statistically significant impact on export performance. In other words, appreciation (depreciation) of real effective exchange rate leads to decrease (increase) in export performance. For Indonesia context, this relationship is crucial due to the tendency of its currency depreciation. On the positive side, 1.74% depreciation of rupiah during 2014 opened an opportunity to increase export performance. Nevertheless, Indonesian export only growth 1% in 2014. Based on this fact, government and business practitioners should find an aggressive and creative way to increase export.

Other factors in this study that affect country's export performance is inflation. Higher inflation can also affect exports by having a direct impact on input costs such as materials and labor. These higher costs can have a substantial impact on the competitiveness of exports in the international trade environment. In Indonesia context, this means government should use monetary policy to ensure that inflation rate is at a safe level.

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