

CHAPTER II

LITERATURE REVIEW

2.1 Theory of International Trade

2.1.1 Theory of Absolute Advantage

The theory of absolute advantage is a theory put forward by Adam Smith in 1776. Adam Smith argues that trade between countries is based on the theory of absolute advantage. This theory explains that a certain country can more efficiently produce a certain commodity when compared to other countries but the country is less efficient in producing certain other commodities. The two countries can benefit by specializing in the production of commodities that have absolute strength and importing commodities that have absolute weaknesses in the country concerned which is capable of producing these commodities more efficiently (Salvatore, 1997).

The theory of absolute advantage provides an explanation that a country can export certain goods because that country is able to produce goods at a lower cost compared to other countries or can be said to have an absolute advantage in producing goods (Marbun, 2015). In addition, Adam Smith argued that absolute advantage can be defined as the ability of a country to produce goods and services per unit by utilizing fewer resources when compared to the capabilities of other countries. Because resources are used more efficiently, the amount of production or goods also increases.

Sampoerna University (2022), explained that there are several main assumptions from the theory of absolute advantage which consist of: (1) Factors of production are only related to labor; (2) The quality of the goods produced has the same value; (3) Exchange of goods regardless of finances; (4) There is no cost of shipping goods in the exchange of goods.

Apart from buying and selling transactions between countries, absolute advantage can also be made by exchanging commodities between countries. The two countries concerned can exchange goods that can only be produced in each country. Exchanges made because the products obtained require a country to incur higher production costs and provide less profit so it is better to import goods to save on production costs.

2.1.2 Theory of Comparative Advantage

The theory of comparative advantage is a theory put forward by David Ricardo in 1817. David Ricardo explained this theory to perfect Adam Smith's theory of absolute advantage. This theory was created to overcome weaknesses in the theory of absolute advantage in countries that do not have absolute advantage. David Ricardo argues that even though a country does not have the ability to produce both commodities efficiently compared to other countries, the country can still carry out mutually beneficial trade. The way that can be done is that a country that is less efficient in producing both commodities needs to specialize in producing and can export the commodity that has the smallest absolute loss or can be called a commodity that has a comparative advantage. In addition, the country must import commodities that have greater absolute weakness or can be called commodities that have comparative weaknesses.

David Ricardo uses several simple assumptions as the basis for the theory of comparative advantage, including: (1) There are only two countries and two commodities; (2) There is free trade; (3) Perfect mobility in factor labor within the country but not freely between the two countries; (4) Production costs that remain unchanged; (5) No shipping or transportation costs; (6) No change in technology.

In the theory of comparative advantage, a resident of a country can improve their standard of living and income if the country specializes in the production of goods or services that have higher productivity and efficiency (Baiza Pariade, 2013). The advantage of the theory of comparative advantage is that it can explain what the exchange rate is and how much the profit is due to exchange where these two things cannot be explained in the theory of absolute advantage (Ibrahim and Halkam, 2021).

2.1.3 Theory Heckscher Ohlin or H-O

This theory was put forward by an economic historian named Eli Heckscher who came from Sweden and his student named Bertil Ohlin in the 1920s. The H-O theory is usually better known as The Proportional Factor Theory. According to this theory, a country can import commodities whose production requires resources that are comparatively difficult to come by and have high prices in that country, while at the same time it can export

commodities whose production levels are higher using production factors that are more plentiful and cheaper in that country (Ibrahim and Halkam, 2021).

According to Heckscher Ohlin's concept, the emergence of international trade is dependent on two key elements: the availability of production inputs and the intensity, or the proportion, of those resources' utilization. The ratios of the production elements will vary depending on the product. Technology defines how to integrate various manufacturing components to create a product, which leads to the differences that occur (Tambunan, 2004). The kinds of goods produced, exported, and goods that a country must import will depend on ownership of resources like labor and capital.

Heckscher Ohlin's theory concludes that trade tends to increase the level of income or wage levels of workers and lower interest rates of real capital in labor-rich and capital-scarce countries. International trade encourages a country to specialize in industry and trade in goods that intensively use the country's excess production factors (Salvatore, 2013). Therefore, it can be concluded that this theory discusses that a country will trade with other countries because the country has a comparative advantage, namely superiority in technology and production factor superiority.

2.2 Literature on Empirical Research

2.2.1 Research on Crude Palm Oil

Crude palm oil is the most vegetable oil-producing plantation commodity so that oil palm plants have very good economic value (Prayitno and Widyawati, 2021). Palm oil is one of the most widely consumed and produced oils in the world. Relatively cheap, easy to produce and highly stable, it is widely used for a wide variety of foods, cosmetics, hygiene products and biodiesel sources, making crude palm oil a widely traded oil (Wicaksono, 2018). Oil palm plants can grow very well in areas that have a tropical climate, this is one of the supporting factors for Indonesia as the largest commodity producer as well as the largest palm oil exporter in the world. Overall, the value of exports from Indonesia starting from January to December 2022 reached US\$291.98 billion, an increase of up to 26.07% when compared to the same period in the previous year (Central Statistics Agency, 2023).

Oil palm is not a plant that originates from Indonesia but originates from West Africa (Supriyono, 2016). Oil palm can develop very rapidly in Indonesia, starting with the Dutch who came to Indonesia bringing 4 palm kernels. In 1848, 4 oil palm seeds were then planted in the Bogor Botanical Gardens. Because Indonesia is a tropical country and oil palm can thrive in a country with a tropical climate, the cultivation of oil palm plants was attempted in several areas so that in 1910, oil palm was finally cultivated commercially and experienced growth expansion to regions in Indonesia. In the 1980s, the area of Indonesian oil palm plantations only reached around 200,000 hectares, most of which were crops inherited from the Dutch colonial government, but over time, in 2009, the area of oil palm plantations in Indonesia reached 7.2 million hectares, and can continue to increase to date (Supriyono, 2016).

2.2.2 Research on The Cause of International Trade

According to Setiawan and Lestari (2011), International trade has several factors that cause buying and selling transactions to be created, including the following:

1. Information revolution and transportation

As time goes by, globalization causes advances in technology and information to develop rapidly, as well as international trade which is growing and facilitating the process of trading activities. Globalization makes it very easy for a country to carry out export and import activities because of the use of information technology that facilitates relations between countries and transportation which speeds up the exchange of goods and services (Azizah, 2021).

2. Interdependence of needs

Each country certainly has advantages and disadvantages in human resources, natural resources, even in information technology, so that the advantages and disadvantages of each country cause a country to depend on other countries to be able to meet domestic needs (Setiawan and Lestari, 2011). Developed countries are more competent in mastering information technology when compared to developing countries. Therefore, developing countries also need developed countries to be able to get easy access to information technology.

3. The principle of comparative advantage

The superiority of a country can be seen from something that is owned by that country but cannot be owned by other countries. The advantages of the country can be a source of more profitable state revenue (Thabroni, 2021).

4. Economic liberalization

Economic liberalization is a policy that plays a major role in driving economic growth and increasing competitiveness. Economic liberation opens enormous opportunities for international business activities so that almost no one avoids this economic policy to seek opportunities by interacting through trade between countries (Thabroni, 2021).

5. The country's foreign exchange needs

The purpose of conducting international trade for a country is to obtain foreign exchange. A country can be said to be good if the country has foreign exchange reserves. This country's foreign exchange reserves have a role to build and develop the country so that to be able to obtain the country's foreign exchange reserves, international trade is needed. Foreign exchange reserves are a very important monetary indicator that shows the strength or weakness of a country's economic fundamentals (Sayoga, et al., 2017).

2.2.3 Research on The Factors of Affecting International Trade

According to the Indonesian Ministry of Education and Culture (2021), there are several things that are affecting factors for international trade, including:

1. Differences in Natural Resources

Each country has natural resource production that varies from one country to another. Indonesia has natural resources such as coffee, palm oil, cocoa, rubber and rubber products and many others. Although Indonesia can produce natural resources in good quantities, Indonesia does not have sufficient ability to be able to process these natural resources so that this becomes one of the driving factors of Indonesia to import natural resources in the form of raw materials to other countries that have sufficient ability to be processed (Ahmad, 2021).

2. Production cost savings

In countries that do not yet have good technology and knowledge in producing their own goods, they will certainly spend higher production costs when compared to these countries buying their goods from other countries that are more competent in producing them. Therefore, buying products that come directly from the country of manufacture can save product costs compared to producing them in their own country (Subroto, 2021).

3. Fulfillment of national needs

There will be times when a particular country will have limitations in meeting all the goods and services that are the needs of its population so that the way the country can meet domestic needs is to buy its needs from other countries or the country needs to import goods and services from abroad (Eirin, 2023).

4. Differences in mastery of technology

The level of mastery of technology in each country that is different will have an impact on production results that are also different. Developed countries with good technological mastery are able to produce modern products in large quantities. These countries need markets to make a profit so they sell these products to developing countries that need their products so that international trade occurs (Thabroni, 2021).

Sukirno and Seregar (2009) stated that there are eight factors that affect international trade, including the following:

1. To satisfy domestic demand for goods and services.
2. The ambition to make money and boost tax income for the government.
3. The capacity to master science and technology in the management of economic resources varies.
4. Domestic products have benefits, but they need a new market.
5. Conditions including natural resources, climate, labor, culture, and population vary, which affects how things are produced and how much can be produced.
6. There is a shared preference for a particular item.
7. The desire to expand political and diplomatic ties as well as receive assistance from other nations.
8. The globalization period makes it impossible for any nation to exist in isolation.

2.2.4 Research on Export Competitiveness

The ability of a commodity to reach foreign markets and the capacity of these commodities to thrive there can be referred to as export competitiveness. A commodity will be in more demand from consumers if it is competitive. (Wardani and Mulatsih, 2017). Basically, the level of competitiveness of a country in the international market can be determined by two factors, namely the comparative advantage factor which can be considered as a natural factor and the competitive advantage factor which can be considered as a factor

that can be developed or created (Tambunan, 2003). . Competitiveness is a general concept used in economics which refers to market competition to the success of competition in international exports (Yulia, et al., 2021). According to the Ministry of Trade (2012), there are two types of trade indices that can be used to measure the level of export competitiveness of a commodity, namely Revealed Comparative Advantage and Trade Specialization Index.

Competitiveness is the relative position of a country compared to other countries. The state has a very important role in increasing competitiveness by creating economic policies and political policies that can benefit the country (Aprilia, et al., 2015). According to Amir in Bustami and Hidayat (2013), that there are three aspects that must be considered by a country in international competition related to commodity export competitiveness, namely (1)the bid price offered by exporting countries has comparative competitiveness if production costs are relatively cheaper than competing countries or prices are also lower or the same as those of destination countries; (2)the quality of the commodities offered must be able to meet and match consumer tastes; (3)delays in shipment and delivery must be adjusted to the situation and conditions that occur in the destination country because delays that occur can be fatal because there is a possibility that the commodity is no longer marketed and can ultimately reduce the demand for the commodity.

2.2.5 International Trade in Crude Palm Oil

Crude palm oil has accounted for about 40% of the supply of the four most popular vegetable oils namely crude palm oil, soybean oil, canola oil, and sunflower seed oil. In the world of international trade, India is the main importer of crude palm oil. China, Pakistan, Bangladesh, Egypt and Kenya are other major buyers. The demand for crude palm oil over the past few years has continued to increase as many developed countries have begun to switch from using trans-fats to healthier alternatives. Products from crude palm oil are products from trans fat substitutes because palm oil is one of the most saturated vegetable fats at a relatively affordable price for all people. World palm oil trade transactions have increased significantly due to rising world demand (Tjahjaprijadi). Quoted from Aflaha, 2022, Malaysia is still the caretaker that determines the ups and downs of the world crude palm oil price through Bursa Malaysia Derivatives. This is because Malaysia was previously the world's largest crude palm oil producer before Indonesia overtook Malaysia's position as the reason for setting reasonable global palm oil prices. On the official website of Bursa

Malaysia Derivatives, crude palm oil trading has been operating since October 1980 which is determined by the Malaysian ringgit and the United States dollar. In addition to being based on Bursa Malaysia Derivatives, the price of crude palm oil also refers to the commodity exchange located in Rotterdam, the Netherlands (Idris, 2022).

