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Impact of Global Financial Crises on National Economic Stagnation

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Abstract

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Global financial crises represent recurrent phenomena that generate systemic risks to national economic stability, particularly in developing economies such as Indonesia. The country's dependence on commodity exports, foreign investment, and its financial sector heightens exposure to international economic disruptions. This study explores the impact of global financial turmoil on the stagnation of Indonesia's economic growth through a literature review. Using a qualitative approach, secondary sources were collected from scholarly journals, books, and international institutional reports. The analysis reveals that crises like the 2008 subprime mortgage collapse and the COVID-19 pandemic triggered a decline in global demand, contraction of exports, withdrawal of foreign capital, and restricted banking liquidity, all of which contributed to stagnation. Critical sectors including manufacturing, property, and banking suffered significant downturns, accompanied by rising unemployment and weakened domestic consumption. Additionally, macroeconomic pressures such as inflation, fiscal deficits, and premature deindustrialization intensified. These findings highlight the importance of adaptive strategies and structural reforms to bolster resilience against future shocks.

1. Introduction

Global financial crises are recurring phenomena that repeatedly disrupt the stability of the international economic system. Over recent decades, the world has faced three major crises with broad systemic implications: the Asian financial crisis of 1997/1998, the U.S. subprime mortgage collapse that evolved into the 2008 global financial crisis, and the COVID-19 pandemic in 2020. Each of these events marks an important milestone in global economic history, illustrating how turbulence in one part of the world can rapidly spill over into other regions. For developing countries with fragile resilience, such as Indonesia, the effects can be particularly severe. The openness of Indonesia's economy, while enabling growth through participation in global trade, foreign investment, and capital flows, simultaneously exposes it to external shocks triggered by instability abroad (Zuhroh & Harpiyansa, 2022). Heavy dependence on export revenues, portfolio inflows, and volatile exchange rates further heightens vulnerability to crises originating in advanced economies, with consequences that often extend into stagnation or prolonged slowdowns in national economic growth (Raihan, 2023).

Economic stagnation, in this context, describes a condition where the Gross Domestic Product (GDP) grows only minimally or remains flat over an extended timeframe. Such stagnation is not limited to poor macroeconomic statistics but extends to social dimensions, as it often undermines welfare indicators and living standards (Khalid et al., 2020). Weak or negative growth translates into the deterioration of real sector activities, increasing unemployment rates, declining purchasing power, and widening social inequality. The study of stagnation thus becomes vital, since global financial crises frequently serve as the initial catalysts. However, attributing stagnation solely to external crises oversimplifies the issue. Domestic structural weaknesses often amplify the severity of global shocks and hinder recovery. Overreliance on less productive sectors, inadequate diversification of the economic base, and shortcomings in fiscal and monetary governance aggravate crisis outcomes. Moreover, inefficiencies in institutional frameworks, bureaucratic inertia, and inconsistencies in policy execution frequently obstruct effective crisis management (Liu & Song, 2020). This interplay suggests that while crises act as triggers, domestic vulnerabilities are the decisive factors that determine the depth and persistence of stagnation.

Although a wide range of academic studies has sought to assess the impacts of global financial crises on individual economies, their scope is often restricted. Many rely on quantitative designs and focus on isolated crisis episodes, leading to fragmented conclusions that lack general applicability. Furthermore, a significant proportion of the literature is concentrated on immediate repercussions in financial markets or banking systems, without fully examining the underlying pathways that translate global shocks into national stagnation. Mechanisms such as declining household consumption, reduced levels of private sector investment, and weakened industrial productivity are sometimes overlooked, despite being central to long-term stagnation dynamics (Paun et al., 2019). The absence of systematic comparison across crises has resulted in a limited understanding of recurring patterns, as well as insufficient differentiation between short-term disruptions and medium- to long-term consequences. Without such synthesis, it becomes difficult to formulate targeted and evidence-based macroeconomic policies that could shield economies like Indonesia's from future turbulence.

To address these shortcomings, this literature review positions itself to provide a comprehensive account of how global financial crises shape the trajectory of national economic stagnation. The study's primary aim is to identify consistent patterns in the impact of crises on key macroeconomic indicators, including GDP performance, investment behavior, household consumption, inflationary pressures, and labor market conditions. By examining existing research through an integrative lens, the review seeks to highlight not only the direct effects of crises but also the structural and institutional factors that aggravate stagnation in developing economies. The synthesis of both theoretical frameworks and empirical studies allows for a more holistic understanding of the mechanisms at play, making it possible to draw broader lessons applicable beyond single episodes or country cases.

Ultimately, the goal of this analysis is to build a solid foundation that future scholars and policymakers can utilize in designing adaptive strategies and long-term reforms. By identifying how crises interact with domestic vulnerabilities to produce stagnation, the study underscores the importance of resilience-oriented policy frameworks. Such strategies might include diversifying economic structures, strengthening fiscal and monetary responses, and improving institutional efficiency to mitigate the fallout from global shocks. Furthermore, a more systematic understanding of crisis–stagnation linkages can help policymakers prepare more effectively for disruptions, minimizing economic instability while supporting sustainable development. In an increasingly interconnected global economy, where shocks spread rapidly across borders, building resilience and ensuring adaptability are essential to safeguarding national growth and welfare.

2. Methods

This research adopts a qualitative methodology, with a literature review serving as the central strategy for data gathering and analysis. The literature review was chosen because it allows for a comprehensive exploration of prior studies, relevant economic theories, and supporting empirical evidence in order to clarify the relationship between global financial crises and national economic stagnation. Such an approach is well suited to the study's purpose of synthesizing and interpreting diverse findings, thereby constructing a more holistic conceptual framework. All data utilized in this study are secondary in nature, obtained from credible references such as textbooks in macroeconomics and international economics, peer-reviewed journals at both national and international levels, and reports issued by globally recognized financial organizations like the World Bank, IMF, and OECD. In addition, the review incorporates academic papers that examine the influence of global crises on economic growth in multiple national contexts, with particular focus on the 1997/1998 Asian financial crisis, the 2008 global financial crisis, and the COVID-19 pandemic of 2020.

The analysis concentrates on two main variables. The independent variable is defined as the global financial crisis, conceptualized as a period of international financial instability that generates major disruptions in markets, capital flows, and global trade. The dependent variable is national economic stagnation, understood as a prolonged weakening or halt of growth, manifested in declining economic activities, shrinking consumption and investment, and rising unemployment levels. This study investigates the interaction between these two variables, assessing how global crises trigger or intensify stagnation both directly, through shocks to trade and finance, and indirectly, through their long-term impacts on structural weaknesses. The investigation further compares different theoretical perspectives and empirical observations from various countries, with emphasis on developing economies such as Indonesia, to identify recurring dynamics as well as country-specific variations.

Data interpretation relies on a descriptive-analytical method, emphasizing the systematic review, interpretation, and extraction of meaning from the selected literature. The collected findings are carefully examined to detect patterns, recurring themes, and explanatory factors that account for the link between crises and stagnation. By combining insights from theoretical discourse with evidence drawn from empirical studies, the research develops an integrated understanding of how global financial instability influences national economic performance. This methodological choice ultimately provides an in-depth perspective on the mechanisms through which international crises generate stagnation, while also offering a valuable basis for subsequent studies and for policy recommendations designed to strengthen resilience against external shocks.

3. Results

3.1. Impact of Global Financial Crises on Indonesia's Key Economic Sectors

Global financial crises, exemplified by the 2008 subprime mortgage collapse and the economic disruption triggered by the COVID-19 pandemic in 2020, create extensive ripple effects that destabilize national economies through channels of trade, investment, and finance. According to Leduc and Liu (2020), these crises affect Indonesia's economic growth by way of both financial and trade linkages. The 2008 crisis, which began with the collapse of the U.S. housing market, produced a sharp decline in global demand for goods and services. Indonesia, with its strong reliance on external trade, experienced a significant downturn in exports of key commodities such as palm oil, coal, and various manufactured products. This contraction in export activities contributed directly to slower Gross Domestic Product (GDP) growth. In addition, the global liquidity crunch that followed reduced foreign direct investment (FDI) and curtailed portfolio inflows, compounding the pressure on the domestic economy. As Li et al. (2022) observe, a worldwide downturn not only constrains trade and investment but also undermines public confidence in domestic markets, intensifying the risk of stagnation.

Liu and Song (2020) emphasize that the consequences of global crises extend well beyond Indonesia's financial system, penetrating into its real economy. Rural households, which depend heavily on agriculture and small-scale trade, are especially susceptible because their livelihoods are tied to markets that are highly responsive to international shifts. For instance, falling international demand for agricultural exports directly lowers farm incomes, reducing household purchasing capacity. This weakening of consumption in rural areas contributes to slower overall economic growth. Sugema points out that the adaptability of rural labor markets, particularly the capacity of workers to move into informal jobs, mitigates some of the employment effects. Nonetheless, even with such flexibility, key sectors lose momentum, slowing national output and growth.

The banking industry, which forms a backbone of Indonesia's financial framework, also suffers heavily from global financial crises. As Khalid et al. (2020) explain, international turbulence tightens liquidity within the banking system. Declining trust in banks, combined with increasing non-performing loans, pushes financial institutions to curtail lending. This contraction in credit particularly impacts industries like manufacturing and property, which rely on bank financing to sustain investment and operations. Reduced lending thereby limits capital formation and stalls productive activities, which in turn deepens stagnation in critical economic sectors. The slowdown in industries dependent on bank loans reflects the broader drag on the nation's growth.

The property sector, with its extensive connections to construction and allied industries, also encounters serious difficulties during global crises. Cheng et al. (2020) argue that higher interest rates set by Bank Indonesia (BI rate) in response to international shocks significantly raise borrowing costs. Elevated credit costs reduce affordability for households, diminish mortgage demand, and hinder repayment capacity. This situation slows property development and directly constrains construction activities, thereby weakening demand for building materials and reducing employment in related industries. The resulting stagnation within the property and construction sectors contributes substantially to the broader national economic deceleration. Cheng further cautions that, without effective and timely government policy responses, such conditions could potentially escalate into an economic crisis of similar magnitude to the Asian financial crisis of 1997/1998.

3.2. Macroeconomic Impacts of Global Financial Crises on Indonesia

The impacts of global financial crises on national economies extend beyond sectoral disturbances, influencing core macroeconomic variables. Makin and Layton (2021) point out that crises tend to intensify pre-existing weaknesses, such as inflationary pressures and fiscal deficits. Drawing on an early crisis detection model, they contend that without timely intervention, Indonesia could face stagflation, marked by sluggish economic growth combined with rising prices. The erosion of investor confidence and turbulence in global financial markets place further strain on the rupiah's exchange rate, heightening import costs and thereby pushing inflation higher. As a result, the competitiveness of Indonesian exports declines, constraining growth prospects and worsening stagnation.

From an Islamic economics lens, the resilience of financial institutions during crises offers significant lessons. Nekhai et al. (2022) demonstrate that sharia banks tend to perform more robustly under crisis conditions compared to conventional banks. The reliance on asset-backed financing and the avoidance of speculative activities, combined with profit-sharing mechanisms, contribute to greater stability in sharia-compliant banking systems. In contrast, conventional institutions, with their deeper exposure to volatile markets, are more susceptible to external shocks. Their findings suggest that adopting Islamic economic principles into broader financial reforms could improve systemic resilience and reduce the likelihood of stagnation.

Arun et al. (2023) further emphasize the decline in foreign capital inflows as a central outcome of the 2008 global financial crisis. The contraction in foreign direct investment (FDI) undermined industrial capacity and manufacturing activity, sectors essential for job creation and technological upgrading. This decline, in turn, magnified stagnation within the national economy. To counter such vulnerabilities, Arun advocates for diversification strategies that expand beyond dependence on external capital, particularly by fostering growth in services and technology-driven sectors. Similarly, Raihan (2023) highlights how global crises weaken Indonesia's balance of payments, primarily through reductions in key commodity exports such as coal and palm oil. Falling international prices diminish state revenues, reduce household purchasing power, and dampen overall economic momentum. Raihan stresses that fiscal reinforcement and structural reforms, particularly improved efficiency within the public sector and diversification of export products, are necessary to mitigate these vulnerabilities.

Regional perspectives also shed light on these dynamics. Zuhroh and Harpiyansa (2022), in examining ASEAN countries including Indonesia, note that global crises disrupt international supply chains, creating significant setbacks for export-oriented industries such as textiles and electronics. Declines in these industries contribute to broader economic stagnation. Hill argues that resilience can be bolstered by pursuing open trade regimes and prioritizing infrastructure investment to enhance competitiveness and global integration. In a similar vein, Mohammed et al. (2021) emphasize that volatility in exchange rates during crises increases the costs of imports while simultaneously undermining export competitiveness. The consequences are particularly severe for manufacturing sectors heavily reliant on global markets. To alleviate these impacts, Basri recommends that Indonesia maintain robust foreign exchange reserves and adopt flexible, responsive monetary policies that can cushion the economy from extended downturns.

The social dimension of crises must also be recognized. Arslan et al. (2021) argue that households engaged in the informal sector suffer disproportionately as both domestic and international demand decline. Stagnation in informal trade and small-scale services exacerbates income inequality and restricts inclusive growth. Expanding microfinance initiatives and strengthening policies that support the informal economy could help mitigate these social imbalances. Additionally, Hynes et al. (2020) show that global financial crises accelerate premature deindustrialization. Investment declines and disruptions in trade reduce the competitiveness of manufacturing, reinforcing dependence on primary sectors like mining. This structural shift leaves the economy increasingly exposed to fluctuations in global commodity prices. In response, Thee recommends prioritizing structural reforms to reinvigorate industrialization while simultaneously promoting diversification across economic sectors.

Taken together, the evidence shows that global financial crises affect national economies through multiple channels, including trade, investment, financial flows, and real sector activity. Declining exports, reductions in FDI, tighter banking liquidity, and falling household purchasing power represent the immediate mechanisms leading to stagnation. At the same time, longer-term consequences include widening inequality and premature deindustrialization, which further constrain development potential. To address these challenges, policy recommendations stress the importance of diversifying economic structures, strengthening foreign exchange reserves, adopting sharia-compliant financial innovations, implementing open trade frameworks, and investing strategically in infrastructure. Through proactive governance and structural transformation, Indonesia can enhance its resilience against global shocks and diminish the likelihood of future stagnation in national growth.

4. Conclusion

Global financial crises have shown wide-ranging and profound consequences for national economies, with developing nations such as Indonesia experiencing particularly severe impacts. These crises influence domestic performance through multiple pathways, including trade, capital flows, financial markets, and overall confidence among economic actors. Declines in international demand lead to falling exports, while contractions in Foreign Direct Investment (FDI) and pressures on financial institutions especially banking and property sectors intensify the economic slowdown. The real sector, especially rural households and workers in informal activities, remains highly exposed to global shocks, resulting in reduced income levels and weakened consumption capacity. The repercussions go beyond immediate disruptions, extending into essential macroeconomic indicators such as rising inflation, volatile exchange rates, fiscal deficits, and increasing social inequality. Over the long term, crises can accelerate premature deindustrialization and erode economic structures, particularly when overreliance on primary commodities is not counterbalanced by industrial upgrading and diversification.

Studies highlight that resilience during crises is shaped by labor market adaptability, the capacity of financial institutions, and the effectiveness of fiscal and monetary measures. Principles of Islamic economics are also recognized as potential stabilizers, as asset-based financing and real sector orientation strengthen systemic durability. To reduce the likelihood of stagnating growth in future crises, Indonesia must adopt adaptive and holistic approaches. Key strategies include advancing economic diversification, building foreign exchange reserves, undertaking structural reforms, enhancing trade and infrastructure connectivity, and fostering informal and value-added sectors. These measures can improve resilience, safeguard sustainable growth, and mitigate the long-term consequences of global financial crises.

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