

THE EFFECT OF INFLATION, MINIMUM WAGE, LABOR ABSORPTION AND THE COVID-19 PANDEMIC ON POVERTY IN INDONESIA

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Abstract

Poverty is still the most important problem in Indonesia, especially in urban areas. The problem of urban poverty is long-term, making it difficult to overcome until now. The increase in urban poverty is often characterized by underdevelopment and backwardness, low productivity and low income received, and the ability and opportunity to develop themselves and improve their welfare. The Covid-19 pandemic also has an impact not only on health but also on urban poverty. There are several factors that cause urban poverty such as high inflation rates, low wages, low employment and Covid-19 Pandemic. The purpose of this study is to determine the effect of Inflation, Minimum Wage, Labor Absorption, and The Covid-19 Pandemic on Urban Poverty in Indonesia. This research uses quantitative methods with multiple linear regression analysis techniques and the Generalized Least Square (GLS) model. This research uses secondary data and the Covid-19 pandemic is categorized as a dummy variable. The results of this study show that inflation has no significant effect on urban poverty. Minimum wage and labor absorption have a negative and significant effect on urban poverty. Meanwhile, the Covid-19 pandemic has a positive and significant effect on urban poverty.

Keywords: Urban poverty, Inflation, Minimum wage, Labor absorption, Covid-19 pandemic

INTRODUCTION

The easiest

Poverty is still the most important social problem in the world. This is evidenced by the fact that poverty is a major goal in the Millennium Development Goals (MGDs) for 2000-2015 that have been agreed upon by 189 UN member states, including Indonesia. Of the eight components of the MDGs, poverty and hunger reduction is the top priority. Based on the evaluation and monitoring of MDG achievements, one of the indicators categorized as red or not yet achieved is poverty reduction (Bappenas, 2024). Urban poverty is a long-term social problem that is difficult to overcome until now. The problem of poverty is often characterized by underdevelopment and backwardness, low productivity and low income received, limited access and ability and opportunity to develop themselves and improve welfare.

In addition, the presence of the Covid-19 pandemic has a negative effect or influence on the supply shock to the economy. Research by Barro et al., (2020) found that the Covid-19 pandemic reduced Gross Domestic Product (GDP) in 2020. The National Bureau of Economic Research (NBER) found that the impact of the Covid-19 pandemic in the United States had an impact on reducing production which had an impact on reducing labor. The decrease in labor has an impact on reducing people's income and increasing poverty (Han et al., 2020).

Nationally, the urban poverty rate in Indonesia increased from 2019-2023, but decreased from 2022-2023. This decline is the result of various government policies that have a good impact on increasing the capabilities of the community.

Table 1. Urban Poor in Indonesia

Year	Poor Population (thousand people)	Percentage of Poor Population (%)
2019	9.994,82	6,69
2020	11.161,96	7,38
2021	12.176,57	7,89
2022	11.820,05	7,50
2023	11.736,36	7,29

Source: Central Buereau of Statistics (2024)

Based on the table above, urban poverty in Indonesia from 2019 to 2023 has increased, from 6.69% in 2019 to 7.29% in 2023. This increase in the poverty rate can be influenced by the high cost of living in a city as a result of unstable inflation, low community income and labor absorption and the impact of the covid-19 pandemic.

Inflation is one of the factors considered to cause an increase in urban poverty in Indonesia. Inflation is an economic situation in which prices rise continuously. According to Fauza (2020) inflation can be said to increase poverty because if inflation occurs the prices of general goods will increase, making it difficult for people to fulfill their basic needs. Thus, it will make people far from prosperous.

In addition to inflation, minimum wage is a factor that affects poverty. In 2019, the average minimum wage in Indonesia was the lowest compared to the year after, which was IDR 2,455,662. Based on the trend of changes in the minimum wage in Indonesia, it has decreased from 8.11% down to 6.63%. According to Muharomi (2022) the minimum wage has the ability to increase the poverty threshold. When the minimum wage is at a low level, the poverty rate increases; conversely, when the minimum wage is high, the poverty rate will decrease. Therefore, it is important for the population to avoid or escape from various poverty conditions.

According to Yustitia et al., (2022), the increase in the number of poor people can be minimized through the expansion of employment opportunities. This is because the breadth of employment can increase the number of working people. If the number of working people increases, it means that there will be many people who have income to meet their basic needs. The trend of employment in urban areas has decreased throughout 2019-2023. In 2019, it was reflected that the percentage of the working population was around 93.71%, which dropped to 93.60% in 2023. Although it tends to increase in 2020-2023, urban labor is still not well absorbed and is still low compared to 2019 before the covid-19 pandemic. There are still many workers who have not been absorbed, resulting in no income.

Based on the description of the problems that have been described, researchers are interested in conducting research on the Effect of Inflation, Minimum Wage, Labor Absorption and The Covid-19 Pandemic on Poverty in Indonesia.

METHOD

The percentage of inflation, the size of the city minimum wage, the number of working people and the number of people living in poverty are the units of analysis used by researchers in this study based on data from the Central Bureau of Statistics and Bank Indonesia.

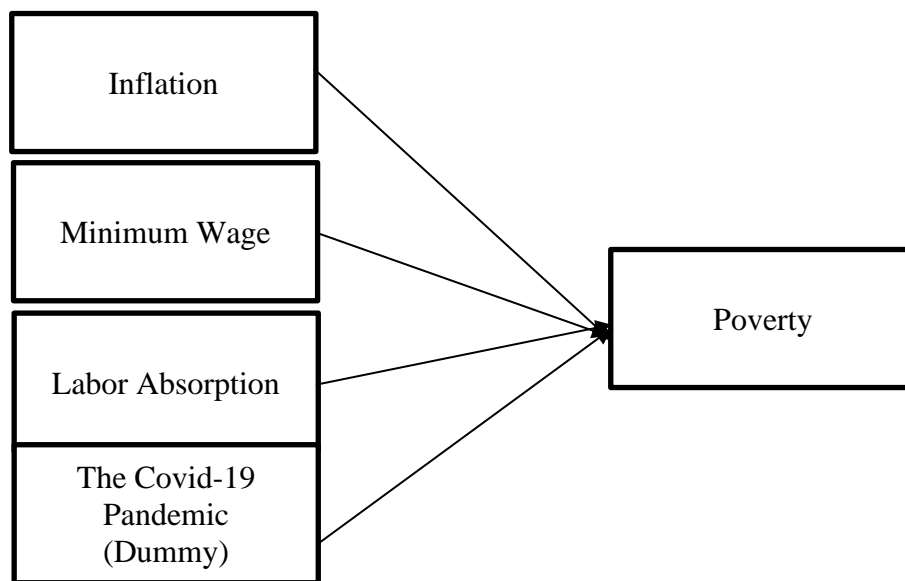


Figure 1. Theoretical Framework

Source: Processed by Researchers

Based on Figure 1, that has been prepared, researchers formulate research hypotheses as follows:

- H1: Inflation has a positive and significant effect on poverty
- H2: Minimum wage has a negative and significant effect on poverty
- H3: Labor Absorption has a negative and significant effect on poverty
- H4: The Covid-19 pandemic dummy has a positive and significant effect on poverty

The panel data regression equation in this study is mathematically, as follows:

$$Y = \alpha + \beta_1 X_{1it} + \beta_2 X_{2it} + \beta_3 X_{3it} + \beta_4 X_{4it} + \epsilon_{it}$$

Description:

Y : Urban Poverty

α : Constant

$\beta_1 \beta_2 \beta_3 \beta_4$: Regression coefficient of each variable

X1 : Inflation

X2 : City Minimum Wage

X3 : Labor Absorption

X4 : Covid-19 Pandemic Dummy

ϵ : error term

i : cross section data

t : time series data

RESULTS AND DISCUSSION

The best model chosen in this study is the Random Effect Model (REM). The following are the panel data regression results with the Random Effect Model (REM) model.

Tabel 2. Regression Model Estimation

Dependent Variable: PV				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	234.2427	71.27595	3.286420	0.0012
INF	-3.447056	3.406848	-1.011802	0.3131
MW	-0.100419	0.027860	-3.604379	0.0004
LA	-0.152832	0.004611	-33.14447	0.0000
COVID	65.71983	13.63738	4.819097	0.0000
R-squared	0.891534			
Adjusted R-squared	0.888904			
F-statistic	339.0518			
Prob(F-statistic)	0.000000			

Source: Processed with Eviews 12 (2024)

Tabel 2 show outcome of the regression equation for the poverty model are obtained as follows:

$$PV = 234.2427 - 3.447056INF - 0.100419MW - 0.152832LA + 65.71983COVID + \epsilon$$

The results of the above equation can be concluded. The P-value of inflation is 0.3131 > 0.05 with a coefficient value of -3.447056. This test result shows that H1 is rejected, there is no significant influence between inflation and urban poverty in Indonesia. Minimum wage has a P-value of 0.0004 < 0.05 with a coefficient value of -0.100419. The test results show that H2 is accepted, there is a negative and significant influence between minimum wage and urban poverty in Indonesia. Labor absorption has a P-value of 0.0000 < 0.05 with a coefficient value of -0.152832. The test results show that H3 is accepted, there is a negative and significant influence between labor absorption and urban poverty in Indonesia. The Covid-19 pandemic has a P-value of 0.0000 < 0.05 with a coefficient value of 65.71983. The test results show that H4 is accepted, there is a positive and significant influence between the Covid-19 pandemic and urban poverty in Indonesia.

The Prob (F-statistic) value is 0.0000, this value is smaller than 0.05 and the F-count is 339.0518 > 2.6590 F-table, it can be concluded that Inflation, Minimum Wage, Labor Absorption, and the Covid-19 Pandemic have a joint effect on Urban Poverty in Indonesia. The R-Squared value is 0.891, meaning that the variables used in this study affect urban poverty in Indonesia by 89.1% and the remaining 10.9% is explained by other variables outside this study.

The Effect of Inflation on Urban Poverty in Indonesia

The test results of the inflation variable on urban poverty show a t-Statistic value of -1.011802 and a probability value of 0.3131 > 0.05. This means that there is a negative and insignificant relationship between the inflation variable and urban poverty. This is certainly not in line with the hypothesis stating that the inflation rate has an influence on the poverty rate and the theory stating that inflation has a positive effect on the poverty rate. This is because the inflation rate will not affect the poor because the poor basically do not have purchasing power, so even though there is inflation they still do not have purchasing power. This research is in line with Gifelem et al., (2023), Teguh & Sinaga (2023) and Rifki Khoirudin & Muhammad Safar Nasir (2022) who also found that inflation has no significant effect on poverty.

In addition, high inflation occurred in 2022-2023 but the poverty rate also decreased. This is because that year was in the recovery phase of the Covid-19 pandemic. The government is targeting to reduce the poverty rate which jumped up in 2020-2021 as a result of the Covid-19 pandemic. The provision of social assistance by the government through Perlinsos by distributing

assistance such as PKH, BPNT, PKH, BLT, KIP, PIP, PBI JKN, and other assistance has succeeded in reducing the urban poverty rate. So, in this case poverty is not only influenced by inflation but the policies carried out by the government in providing social assistance also affect the poverty rate. Although in this case inflation does not have a significant effect, the government must still maintain price stability so that inflation is well controlled and does not increase the poverty rate.

The Effect of Minimum Wage on Urban Poverty in Indonesia

The test results of the city minimum wage variable on urban poverty show a t-Statistic value of -3.604379 and a probability value of $0.0004 < 0.05$, meaning that there is a negative and significant relationship between the minimum wage variable and urban poverty. The provision of the city minimum wage aims to improve the welfare of workers in the city area. This research is in line with research from Permana & Pasaribu (2023) and Priseptian & Primandhana (2022).

It is also in accordance with the natural wage theory which explains that if the wage level increases, welfare will increase and poverty will decrease. Thus, an increase in the minimum wage can be one of the strategies to reduce poverty in Indonesia, assuming that the increase is in accordance with economic conditions and does not cause other negative impacts.

The Effect of Labor Absorption on Urban Poverty in Indonesia

The test results of the labor absorption variable on urban poverty show a t-Statistic value of -33.14447 and a probability value of $0.0000 < 0.05$, meaning that there is a negative and significant relationship between the labor absorption variable and poverty. This research is supported by research from Yustitia et al., (2022) and Pamuji (2019). In accordance with Nurkse's theory which states that the low process of job creation can result in low labor absorption and high poverty rates due to the absence of income to meet their basic needs. The formal sector still dominates employment in urban Indonesia. Effective strategies are needed to continue to encourage an increase in the number of workers such as providing skills training as a workforce readiness. In addition, encouraging the development of MSMEs and investment to create jobs.

The Effect of Covid-19 Pandemic on Urban Poverty in Indonesia

The test results of the Covid-19 pandemic dummy variable on urban poverty show a t-Statistic value of 4.819097 and a probability value of $0.0000 < 0.05$, meaning that there is a positive and significant relationship between the Covid-19 pandemic variable and urban poverty. The results of this study are supported by the research of Anser et al., (2020) and Barro et al., (2020) which show that the Covid-19 pandemic has caused a decrease in consumption and economic growth. The Covid-19 pandemic has an impact on reducing economic activity, thereby reducing consumption and investment levels. Poverty is characterized by the absence of welfare in society so that the low level of consumption affects the poverty rate.

CONCLUSION

Based on the findings of this study, it can be concluded that inflation has no significant effect on urban poverty. Minimum wage has a negative and significant effect on urban poverty. Labor absorption has a negative and significant effect on urban poverty. The Covid-19 pandemic has a positive and significant effect on urban poverty. Inflation, minimum wage, labor absorption and the Covid-19 pandemic together affect urban poverty in Indonesia.

Based on the findings of this study, it is recommended that the government can keep the inflation rate stable through policies that will be implemented. In increasing the minimum wage, the government must also be careful in issuing policies and carried out gradually and the government must focus on implementing policies for the job creation process. The recommendations for future research are expected to extend the research period and consider other variables that affect urban poverty.

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