

Deglobalization and Protectionism: Implications for Indonesia's Economic Stability and National Resilience

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ABSTRAK

This research examines the intricate interplay among geopolitical risk, the quality of democracy, financial sector stability (specifically non-performing loans), and macroeconomic stability (inflation) on regional economic growth across Indonesia. While these factors have been extensively investigated in isolation, a comprehensive panel data analysis that integrates these diverse elements, particularly within the dynamic context of Indonesia's regional economy, remains underexplored. The primary objective of this study is to empirically analyze the short-term and long-term impacts of Geopolitical Risk (GPR), the Democracy Index (DI), Non-Performing Loans (NPL), and the Inflation Rate (IR) on Gross Domestic Regional Product Growth (GDRPG) across all provinces in Indonesia. Utilizing panel data from Indonesian provinces, this study employs the Generalized Method of Moments (GMM) regression, a robust econometric technique specifically designed for dynamic panel data models to address issues of endogeneity and unobserved heterogeneity. For comparative analysis and robustness validation, Partial Least Squares (PLS) and Fixed Effects Model (FEM) regressions were also conducted. The GMM results indicate that lagged regional economic growth exerts a significant and positive influence on current growth. Interestingly, Geopolitical Risk (GPR) and the Inflation Rate (IR) were found to have a significant positive impact on GDRPG, whereas the Democracy Index (DI) and Non-Performing Loans (NPL) demonstrated a significant negative impact. Diagnostic tests confirmed the validity and efficiency of the GMM model. These findings offer crucial implications for policymakers in formulating targeted strategies to foster sustainable regional economic growth, underscoring the necessity for robust financial sector management, prudent macroeconomic policies, and adaptive responses to evolving geopolitical dynamics.

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1. INTRODUCTION

The global economy is currently undergoing a fundamental paradigm shift, transitioning from an era of hyper-globalization towards a landscape increasingly defined by deglobalization and protectionism. This phenomenon is more than a mere cyclical economic fluctuation; it is a direct consequence of escalating geopolitical tensions, the vulnerabilities of global supply chains exposed by the COVID-19 pandemic, and the resurgence of economic nationalism across various parts of the world. The emergence of these factors has prompted a re-evaluation of global economic integration (Kim et al, 2020).

Armed conflicts, intensified strategic competition among major powers, and increasingly restrictive trade policies have collectively generated profound uncertainty, disrupted established international trade patterns, and triggered volatility in global financial markets.² For developing nations, including Indonesia, this transformative shift presents a complex duality of both formidable challenges and unique opportunities. As one of Southeast Asia's largest economies, with a substantial reliance on international trade and foreign investment, Indonesia finds itself at the forefront of deglobalization's profound impact. Protectionist measures, such as the imposition of increased tariffs and non-tariff barriers, have the potential to restrict market access, impede innovation, and diminish the competitiveness of domestic industries (Egan & Roche, 2025). Conversely, deglobalization can also serve as a catalyst, encouraging the strengthening of domestic industries, fostering the diversification of supply chains, and enhancing national economic resilience through a renewed focus on domestic production and a reduction in external dependencies (Sustainable Trade and Finance, 2025).

Indonesia has demonstrated remarkable economic resilience, consistently maintaining a stable economic growth rate of approximately 5% per year, even amidst significant global turmoil (Zaza et al, 2025). This resilience is primarily underpinned by robust domestic consumption, a persistent trade balance surplus, and a prudent macroeconomic policy framework. Nevertheless, the Indonesian economy is not entirely impervious to external pressures. The depreciation of the Rupiah against the US Dollar and a discernible declining trend in the trade balance surplus highlight the inherent domestic vulnerabilities to global shocks (Nota Keuangan APBN 2025).

The financial sector plays a pivotal role in supporting a nation's economic growth, acting as an efficient intermediary for capital allocation and investment facilitation (OJK, 2025). Consequently, safeguarding the stability and resilience of the financial sector is paramount, particularly when confronting external shocks stemming from geopolitical tensions and shifts in trade policies. Institutions such as the Financial Services Authority (OJK) and Bank Indonesia (BI) are actively engaged in maintaining the stability of Indonesia's financial system through the implementation of various macroprudential policies and stringent oversight (Kemenkeu, 2025).

The increasing global interconnectedness implies that geopolitical risks do not solely impact the directly involved nations but also propagate through various channels to domestic economies. These channels include trade flows, investment flows, and overall financial market sentiment (bca.go.id, 2025).

Within this intricate framework, the financial sector functions as a critical conduit that can either amplify or mitigate the effects of such shocks. A profound comprehension of how deglobalization and protectionism, as reflected by geopolitical risk, influence economic growth at the provincial level in Indonesia, while considering the role of democratic institutional quality, the health of the financial sector (proxied by Non-Performing Loans/NPL), and inflation, is indispensable for formulating adaptive and strategically sound policies.

This research endeavors to address a notable gap in the existing literature by empirically analyzing the combined impact of geopolitical risk, the democracy index, NPL, and inflation on economic growth at the provincial level in Indonesia. By employing dynamic panel data and the Generalized Method of Moments (GMM) methodology, this study aims to provide more nuanced perspectives on how global and domestic factors interact to shape the trajectory of economic growth across Indonesia's diverse regions amidst the ongoing era of deglobalization and protectionism. The unique economic characteristics and policy responses of Indonesia warrant a detailed investigation into these complex relationships.

2. LITERATURE REVIEW

2.1. Deglobalization and Protectionism

Deglobalization is conceptualized as the inverse of globalization, representing a process characterized by diminishing interdependence and integration among global entities, particularly nation-states. This phenomenon manifests through a reduction in international trade and investment flows, a rise in regionalism, and a discernible trend towards the localization or regionalization of supply chains (Sustainable Trade and Finance, 2025). The primary forces driving deglobalization are multifaceted, encompassing trade imbalances, mounting political pressures, the rise of populism, persistently high unemployment rates, escalating trade tensions between countries, and the vulnerabilities within global supply chains that were starkly revealed during the COVID-19 pandemic (Kim et al, 2020).

Protectionism, an economic policy centered on fostering domestic production and consumption to achieve self-sufficiency and reduce reliance on foreign markets, frequently emerges as a pivotal tool in an era of deglobalization (Economic Nationalism, 2025). Protectionist measures, such as tariffs and quotas, are strategically employed to shield domestic industries from intense foreign competition. While such policies can safeguard domestic employment and industries, they concurrently carry the inherent risk of provoking retaliatory measures from other countries, which can lead to increased consumer prices and a reduction in overall global economic efficiency. The interplay between these drivers and policy responses shapes the evolving global economic landscape (Egan & Roche, 2025; Qiu et al, 2024).

2.2. Geopolitical Risk (GPR) and its Impact on the Economy

Geopolitical risk (GPR) pertains to the academic discipline that investigates how geographical, political, and economic factors collectively influence a nation's foreign policy and its assertion of state power. The recent

surge in global geopolitical tensions, exemplified by armed conflicts and heightened strategic competition among nations, has generated serious apprehension regarding global economic and financial stability (bca.go.id, 2025).

The mechanisms through which geopolitical tensions transmit their effects to the broader economy are diverse and interconnected. Firstly, increased global political risk can significantly amplify volatility within domestic financial markets, erode investor confidence, and impede the inflow of foreign direct investment (FDI) (Larasati, 2025). Secondly, shifts in geopolitical dynamics, including economic fragmentation and the rise of protectionism, directly influence international trade patterns, impacting a country's export and import volumes (Asrini et al, 2025). Thirdly, geopolitical conflicts frequently precipitate supply or demand shocks that lead to sharp increases in the prices of key commodities, which can subsequently trigger inflationary pressures. Lastly, the pervasive uncertainty engendered by geopolitical developments often elicits adverse reactions in both global and national markets, resulting in currency depreciation and an escalation in government bond yields. Despite these manifold challenges, Indonesia has demonstrated a notable degree of economic resilience in sustaining foreign direct investment inflows amidst global uncertainties. This suggests that countries possessing robust economic fundamentals and adaptive policy frameworks can either mitigate the adverse effects of GPR or, in certain circumstances, attract investment as a "safe haven" during periods of heightened global instability (Caldara & Matteo, 2022).

2.3. Democracy Index (DI) and Economic Growth

The relationship between democracy and economic growth is a subject of considerable complexity and ongoing debate within economic literature. Theoretically, well-established democratic institutions, coupled with robust civil liberties and political rights, are posited to contribute positively to economic growth. This positive contribution is often attributed to enhanced governmental accountability, stronger protection of property rights, reduced levels of corruption, and increased public participation in economic decision-making processes. Countries that possess strong civil liberties, provided they are capable of effectively controlling and consolidating their democratic framework, tend to exhibit higher economic returns (Purba & Hariyadi, 2023).

However, empirical research conducted in Indonesia presents a more nuanced and sometimes contradictory picture. Several studies have indicated that Indonesia's Democracy Index (IDI) either has no statistically significant effect on economic growth across its provinces or, in some instances, even shows a negative correlation. A frequently cited explanation for these divergent findings is the pervasive presence of multi-layered and persistent corruption practices, alongside the suboptimal quality of institutional governance. These systemic issues are believed to impede the creation of an environment conducive to robust economic activity, investment, and capital flows (Adip et al, 2019). This suggests that the mere existence of formal democratic processes may not be sufficient; rather, the qualitative aspects of democratic

governance, including the effective enforcement of law and a high degree of transparency, are likely more critical determinants of economic prosperity.

2.4. Non-Performing Loan (NPL) and Economic Growth

The Non-Performing Loan (NPL) ratio, or the proportion of problematic loans, serves as a crucial indicator of the overall health of the banking sector and, by extension, the resilience of the financial sector as a whole. A high NPL ratio signifies that a substantial portion of bank loans are unlikely to be repaid, which in turn diminishes the capacity of banks to extend new credit, thereby hindering investment and ultimately decelerating economic growth (Wardani & Haryanto, 2021). Thus, NPL functions as a direct proxy for the financial sector's well-being.

In Indonesia, the aggregate NPL ratio for the banking sector has generally been maintained below the 5% threshold, which is indicative of the financial sector's relative stability. This consistently low and well-managed NPL level suggests that Indonesia's financial sector possesses a sufficiently robust foundation to effectively support economic activity (Chase-dun et al, 2023). Nevertheless, fluctuations in NPL ratios remain pertinent, as they can influence the financial intermediation function and the overall capacity of banks to facilitate and sustain economic growth.

2.5. Inflation (IR) and Economic Growth

The relationship between inflation and economic growth is complex and often characterized as bidirectional. High rates of inflation can be detrimental to economic growth by eroding the purchasing power of the populace, discouraging investment due to heightened uncertainty, and increasing production costs for businesses. Conversely, a low and stable inflation rate is generally considered conducive to fostering economic growth (Nahdirin, 2017). Inflation, therefore, is an important barometer of macroeconomic stability. In the prevailing context of escalating geopolitical tensions and the trend towards deglobalization, global commodity price shocks can directly trigger domestic inflationary pressures, thereby creating a negative feedback loop that can impede economic growth. Understanding this dynamic is crucial for effective macroeconomic management (Nota Keuangan APBN 2025).

3. METHOD, DATA, AND ANALYSIS

3.1. Research Design

This research employs a quantitative approach utilizing a panel data study design. The selection of panel data is advantageous as it facilitates the analysis of variable dynamics over time (time series dimension) while simultaneously capturing the inherent heterogeneity across observational units (cross-section dimension). This design is particularly well-suited for investigating causal relationships and policy impacts within the context of regional macroeconomics. It enables researchers to effectively control for unobserved province-specific effects and address endogeneity issues, which are frequently encountered in economic data analysis.

3.2. Data and Data Sources

The dataset employed in this study is a balanced panel, encompassing 34 provinces across Indonesia over a 12-year period, from 2013 to 2024. It is important to note that while Indonesia currently comprises 38 provinces, this research specifically focuses on the 34 provinces that have maintained consistent administrative existence throughout the 2013-2024 timeframe. This deliberate selection ensures the integrity and comparability of the panel data, which is crucial for robust econometric analysis. The definitions of the variables and their primary data sources are presented in Table 1.

Table 1. Variable Definitions and Data Sources

Variable	Definition	Unit of Measurement	Main Data Source
Dependent Variable (Y)			
Economic Growth (GDRPG)	Growth rate of Gross Regional Domestic Product (GRDP) per capita at constant prices per province.	Percent (%)	Central Bureau of Statistics (BPS)
Independent Variables (X)			
Geopolitical Risk (GPR) Indonesia (X1)	Index measuring the level of geopolitical tension and uncertainty at the national level (as a proxy for provinces).	Index (e.g., 1985-2019 = 100)	Caldara and Iacoviello (www.matteoiacoviello.com/gpr.htm) or other sources that provide relevant national GPR data for Indonesia
Democracy Index (DI) (X2)	Composite index measuring the level of democratic development in each province, encompassing aspects of civil liberties, political rights, and the capacity of democratic institutions.	Points (0-100)	Central Bureau of Statistics (BPS) annual publication of the Indonesian Democracy Index (IDI) per province
Control Variables			
Non-Performing Loan (NPL) (Control 1)	Ratio of non-performing loans in the national banking system (as a proxy for provinces).	Percent (%)	Financial Services Authority (OJK) / Bank Indonesia (BI) Indonesian Banking Statistics, national level
Inflation (IR) (Control 2)	Annual inflation rate per province, measured by the Consumer Price Index (CPI).	Percent (%)	Central Bureau of Statistics (BPS) annual CPI inflation publication per province

It is important to acknowledge that specific and consistently available provincial-level data for Geopolitical Risk (GPR) and Non-Performing Loans (NPL) for such an extended period are generally not publicly accessible. Consequently, this study employs the national GPR index as a proxy for provincial GPR. The justification for this approach is rooted in the understanding that major geopolitical events, such as global conflicts or trade wars, tend to exert widespread systemic and national impacts, even if their regional manifestations may vary. Similarly, aggregate NPL data for the entire banking sector at the provincial level are challenging to obtain consistently. Therefore, national NPL data are utilized as a proxy for provincial NPL, operating under the assumption that provincial NPL movements largely mirror national trends or that the impact of NPL is relatively uniform across provinces. These inherent data limitations are duly recognized and will be further addressed in the discussion section.

3.3. Empirical Model

This study aims to estimate the relationships between geopolitical risk, the democracy index, NPL, and inflation on provincial economic growth using a dynamic panel data regression model. This particular model specification is chosen because it incorporates a lagged dependent variable as one of the predictors, which is essential for capturing the persistence effects or the adjustment dynamics of economic growth over time. The general form of the empirical model to be estimated is specified as follows:

$$GDRPG_{it} = \beta_0 + \beta_1 GDRPG_{it-1} + \beta_2 GPR_{it} + \beta_3 DI_{it} + \beta_4 NPL_{it} + \beta_5 IR_{it} + \mu_{it}$$

Where:

- GDRPG_{it} : represents the Economic Growth of Province *i* in year *t*.
- GDRPG_{it-1} : denotes the Economic Growth of Province *i* in year *t-1* (serving as the lagged dependent variable).
- GPR_{it} : signifies the Geopolitical Risk in Indonesia in year *t*.
- DI_{it} : refers to the Democracy Index of Province *i* in year *t*.
- NPL_{it} : indicates the Non-Performing Loan in year *t*.
- IR_{it} : denotes the Inflation of Province *i* in year *t*.
- β₀ : is the constant term.
- β₁, β₂, ..., β₅ : represent the regression coefficients to be estimated, quantifying the impact of each respective variable on economic growth.
- μ_i : captures the unobserved individual (province-specific) effects, accounting for unique characteristics of each province that remain constant over time.
- ε_{it} : is the error term, capturing variations not explained by the variables included in the model.

3.4. Analysis Method

Dynamic panel data models, by their very nature, include a lagged dependent variable (GDRPGit-1), which inherently introduces endogeneity issues due to its correlation with the unobserved province-specific effects (μ_i). In this context, the application of standard estimation methods, such as Ordinary Least Squares (OLS) or Fixed Effects (FE), would yield biased and inconsistent estimates. Furthermore, potential endogeneity may also arise from other explanatory variables (e.g., GPR or NPL) in relation to economic growth, where the causal relationship could be bidirectional or driven by common unobserved factors.

To effectively address these pervasive endogeneity problems inherent in dynamic panel models, as well as potential endogeneity in the explanatory variables, the Generalized Method of Moments (GMM) stands as the most appropriate econometric technique. GMM is specifically designed to handle unobserved heterogeneity across units (provinces) and endogeneity issues by strategically employing internal instruments, which are typically lagged values of the dependent variable and other explanatory variables. This study will specifically utilize the System GMM approach (Arellano-Bover/Blundell-Bond), which is generally considered more efficient than Difference GMM, as it leverages additional instruments for the level equation, thereby enhancing the precision of the estimates.

To ensure the validity and reliability of the GMM estimation results, several critical diagnostic tests will be performed:

- Sargan/Hansen Test. This test is employed to assess the validity of the instruments (over-identifying restrictions) used in the model. The null hypothesis (H_0) for this test posits that the instruments are valid and uncorrelated with the error term. A failure to reject H_0 indicates that the selected instruments are appropriate for the model.
- Arellano-Bond Test (AR(1) and AR(2)). This test is conducted to examine the presence of autocorrelation in the first-differenced errors. For consistent GMM estimation, first-order autocorrelation (AR(1)) is expected in the first-differenced errors due to the differencing process itself. However, the absence of second-order autocorrelation (AR(2)) is crucial. A failure to reject H_0 for AR(2) signifies that the model has been correctly specified and that the instruments employed are suitable.

4. RESULT AND DISCUSSION

The analysis of the data was conducted using the Generalized Method of Moments (GMM) method, with results presented through Stata output. The following sections detail the descriptive statistics, correlation matrix, and the GMM estimation results, along with their interpretations regarding the influence of various variables on provincial economic growth in Indonesia.

4.1. Descriptive Statistics

The descriptive statistics provide an initial overview of the dataset's characteristics.

Table 2. Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
GDRPG	408	3.48	3.82	-20.13	21.18
GPR	408	0.04	0.05	0	0.18
DI	408	73.97	6.55	52.61	89.21
NPL	408	220.62	533.13	0	5530.66
IR	408	3.90	2.51	-0.02	15.61

From Table 2, it is observed that the average provincial economic growth (GDRPG) is 3.48% with a standard deviation of 3.82%. This standard deviation indicates a considerable degree of variation in economic growth rates across different provinces and over the observed time period. The Democracy Index (DI) exhibits an average score of 73.97, suggesting a generally "moderate" level of democratic development across Indonesia. The Non-Performing Loan (NPL) ratio, reported as an absolute value rather than a percentage, has an average of 220.62. Its exceptionally high standard deviation of 533.13 points to a very wide dispersion of data points for this variable, potentially indicating significant outliers or a skewed distribution in the absolute NPL values. The average inflation rate (IR) stands at 3.90% with a standard deviation of 2.51%.

4.2. Matrix Correlation

The correlation matrix provides insights into the initial linear relationships between the variables.

Table 3. Matrix of Correlations

Variables	GDRPG	GPR	DI	NPL	IR
GDRPG	1.000				
GPR	0.158	1.000			
DI	-0.016	0.246	1.000		
NPL	-0.018	0.109	0.190	1.000	
IR	0.138	0.199	-0.232	-0.121	1.000

Table 3 reveals that Geopolitical Risk (GPR) has a weak positive correlation with GDRPG (0.158). In contrast, the Democracy Index (DI) and Non-Performing Loans (NPL) show very weak negative correlations with GDRPG (-0.016 and -0.018, respectively). Inflation (IR) exhibits a weak positive correlation with GDRPG (0.138). These initial low correlation coefficients for DI and NPL with GDRPG suggest that simple linear relationships may not fully capture their influence. This observation underscores the necessity of employing a more sophisticated dynamic panel data model, such as GMM, which can account for complex relationships, including dynamic effects and potential endogeneity, that simple correlations cannot reveal. A multicollinearity test was also performed, showing Variance Inflation Factor (VIF) values below 10 for all variables, with a Mean VIF of 1.14. This indicates the absence of serious

multicollinearity issues within the model, which is a favorable condition for the reliability of the regression estimates.

4.3. GMM Estimation Results

The primary empirical results are derived from the Generalized Method of Moments (GMM) estimation, which is deemed the most appropriate method for this dynamic panel data analysis.

Table 4. GMM Estimation

GDRPG	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]	Sig
L.GDRPG	0.179	0.006	31.09	0.000	0.168	0.191	***
GPR	12.689	0.247	51.37	0.000	12.187	13.192	***
DI	-0.023	0.006	-3.51	0.001	-0.036	-0.010	***
NPL	0.0001	0.000	-3.16	0.003	0.000	0.000	***
IR	0.114	0.006	18.34	0.000	0.101	0.126	***
Constant	3.589	0.485	7.40	0.000	2.603	4.577	***
Mean dependent var			3.396	Prob > F			0.000
Number of obs			374	Arellano-Bond AR(1)			0.000
Hansen test			0.985	Arellano-Bond AR(2)			0.847

*** $p < .01$, ** $p < .05$, * $p < .1$

The diagnostic tests for the GMM model confirm its validity and consistency. The Hansen test yielded a p-value of 0.985, which is substantially above the 0.10 significance level, indicating that the instruments employed in the model are valid and appropriately specified. Furthermore, the Arellano-Bond AR(2) test resulted in a p-value of 0.847, also well above 0.10. This outcome signifies the absence of second-order autocorrelation in the differenced error term, which is a critical condition for the consistency of GMM estimates. The presence of AR(1) ($p=0.000$) is expected and does not invalidate the model.

For a comprehensive assessment and robustness check, the results from Partial Least Squares (PLS) and Fixed Effects Model (FEM) regressions are also presented in Table 1 below, allowing for a direct comparison with the GMM findings.

Table 5. PLS, FEM, dan GMM

Variable	PLS		GMM		FEM	
	Coef.	St.Err	Coef.	St.Err	Coef.	St.Err.
L.GDRPG			0.179***	0.006		
GPR	11.017***	3.972	12.689***	0.247	12.650***	3.924
DI	-0.015	0.031	-0.023***	0.006	-0.052	0.043
NPL	0.0001	0.000	0.0001***	0.000	0.0001	0.001
IR	0.153*	0.079	0.114***	0.006	0.120	0.079
constant	3.546	2.355	3.589***	0.485	6.402**	3.224
Prob > F	0.004		0.000		0.000	
R-squared	0.038				0.049	
Hansen test			0.985			
Arellano-Bond AR(2)			0.847			

*** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

Source: Author's Computation Using Stata 17

The comparison across models reveals broad consistency in the direction and significance of some key variables, particularly for GPR. However, differences in significance for DI and NPL across models underscore the importance of GMM's ability to handle endogeneity and unobserved heterogeneity, validating its choice as the primary estimation method.

4.4. Interpretation of GMM Results

Lagged Economic Growth (L.GDRPG). The coefficient for L.GDRPG is 0.179, with a p-value of 0.000, indicating a positive and statistically significant influence at the 1% level. This finding suggests that provincial economic growth from the previous year has a positive and persistent effect on economic growth in the current year. This is consistent with the dynamic nature commonly observed in economic growth patterns, where momentum from one period tends to carry over into the subsequent period. The significance of this lagged variable validates the use of a dynamic panel model, confirming that past economic performance is a crucial determinant of current growth.

Geopolitical Risk (GPR). The coefficient for GPR is 12.689, with a p-value of 0.000, indicating a positive and statistically significant influence at the 1% level. This result initially appears surprising and counterintuitive, as it suggests that an increase in geopolitical risk is positively correlated with economic growth in Indonesian provinces. However, this finding can be understood within the unique context of deglobalization and protectionism. One possible explanation is Indonesia's position as a beneficiary amidst global uncertainty and the fragmentation of supply chains. As a major producer of key commodities such as nickel, coal, and natural gas, and possessing a substantial domestic market, Indonesia may gain from shifts in investment or the diversification of supply chains away from more vulnerable economies. Rising commodity prices, often a consequence of heightened geopolitical tensions, can also significantly boost Indonesia's export revenues (Wang et al, 2023; Hutasiot et al, 2024).

Furthermore, Indonesia has demonstrated robust domestic economic resilience, supported by its large domestic consumption base and a prudent macroeconomic policy framework. This inherent stability may render Indonesia a relatively more attractive destination for investors compared to other countries that are more severely impacted by geopolitical turmoil. The GPR index itself primarily measures market attention to geopolitical risk. Therefore, an increase in this index, reflecting heightened market awareness of global risks, might coincidentally occur during periods when Indonesia is strategically positioned to capitalize on emerging opportunities, such as industrial relocation or increased investment in strategic sectors that become focal points amidst deglobalization trends. This suggests that while global risk perception may rise, Indonesia's adaptive capacity allows it to navigate and even benefit from these shifts (Sitorus et al, 2024; Saputra et al, 2024).

Democracy Index (DI). The coefficient for DI is -0.023, with a p-value of 0.001, indicating a negative and statistically significant influence at the 1% level. This finding is also counterintuitive when viewed against the general theoretical premise that robust democratic institutions foster economic growth.

Nevertheless, this result aligns with several prior empirical studies conducted in Indonesia, which have similarly found that Indonesia's Democracy Index (IDI) either has no significant effect or a negative effect on economic growth. A plausible explanation for this observed negative correlation is that despite Indonesia's successful establishment of a modern, formal democratic system, underlying issues persist. These include entrenched and continuous corruption practices, alongside a suboptimal quality of institutional governance. Such systemic deficiencies may impede democracy from effectively cultivating a conducive environment for economic activity, investment, and capital flows. This implies that the mere presence of democratic processes is insufficient; rather, the qualitative aspects of democratic governance, particularly the strength of law enforcement and the degree of transparency, appear to be more critical factors in driving economic prosperity than a formal democracy score alone (Adip et al, 2019; Goldberg et al, 2023).

Non-Performing Loan (NPL). The coefficient for NPL is 0.0001, with a p-value of 0.003, indicating a positive and statistically significant influence at the 1% level. While this finding is statistically significant, the coefficient's value is extremely close to zero, which suggests that the impact of NPL on provincial economic growth is economically negligible or practically insignificant. Theoretically, a high NPL ratio is expected to impede economic growth by constraining banks' lending capacity and dampening investment. However, considering that the aggregate NPL ratio for the banking sector in Indonesia has generally been maintained below the 5% threshold, it indicates that Indonesia's financial sector is relatively stable and adept at managing credit risk. Consequently, the overall impact of NPL on macroeconomic growth at the provincial level becomes minimal. The very small positive coefficient observed might also reflect a dynamic where periods of robust economic growth lead to an expansion in overall credit activity. While this credit expansion is generally healthy, it can, in absolute terms, slightly increase the volume of non-performing loans, even as the NPL ratio remains low and well-controlled. This interpretation reconciles the statistical significance with the economic insignificance of the finding (Wardani & Haryanto, 2021; Hidayaturrehman et al, 2024).

Inflation (IR). The coefficient for IR is 0.114, with a p-value of 0.000, indicating a positive and statistically significant influence at the 1% level. This result suggests that an increase in inflation is positively correlated with provincial economic growth. This finding can be explained by the theory of demand-pull inflation, where strong economic growth and an increase in aggregate demand naturally lead to upward pressure on prices. Moderate and controlled inflation is often considered a hallmark of a healthy and dynamic economy, as it reflects vibrant economic activity and sustained purchasing power within the populace. However, it is crucial to recognize that while moderate inflation can be benign, excessively high or uncontrolled inflation can severely undermine economic growth in the long run by eroding real incomes and creating significant economic uncertainty. Therefore, the positive correlation observed should be interpreted within the context of managed inflationary pressures that accompany economic expansion (Nahdirin, 2017).

5. CONCLUSION AND SUGGESTION

This research systematically investigated the impact of geopolitical risk, the democracy index, Non-Performing Loans (NPL), and inflation on economic growth across 34 provinces in Indonesia during the 2013-2024 period, employing the Generalized Method of Moments (GMM) methodology. The study yields critical insights into Indonesia's economic dynamics amidst the evolving era of deglobalization and protectionism.

The findings reveal a significant persistence in provincial economic growth, indicating that growth achieved in the preceding year tends to carry forward into the subsequent year.¹ A notable and somewhat unexpected finding is the positive and significant influence of increased geopolitical risk on provincial economic growth in Indonesia. This suggests that amid the global pivot towards deglobalization and protectionism, Indonesia may be uniquely positioned to benefit, either as an alternative destination for investment or through the appreciation of commodity prices driven by global tensions. This outcome underscores Indonesia's inherent economic resilience and adaptive capacity in a turbulent global environment.

Conversely, the Democracy Index per province was found to exert a negative and significant influence on economic growth. This outcome highlights that despite Indonesia's adoption of a modern democratic system, persistent challenges related to the quality of institutions, the effectiveness of law enforcement, and the systematic eradication of corruption may still impede democracy from optimally fostering economic growth at the regional level.

Regarding Non-Performing Loans, while their impact on economic growth was statistically significant, its magnitude was found to be very small and positive. This indicates that Indonesia's financial sector maintains a relative degree of stability and demonstrates a robust capacity for managing credit risk effectively. Consequently, NPLs do not appear to pose a significant impediment to aggregate economic growth at the provincial level. Lastly, inflation was found to have a positive and significant influence on economic growth. This can be interpreted as demand-pull inflation, where moderate price increases are a natural accompaniment to a growing economy, reflecting healthy economic activity.

6. POLICY RECOMMENDATIONS

Based on these empirical findings, several targeted policy recommendations can be formulated to bolster Indonesia's economic stability and national resilience amidst the continuously evolving global landscape:

- **Leveraging Deglobalization Opportunities.** The government should proactively identify and strategically capitalize on the opportunities arising from the prevailing trends of deglobalization and protectionism. This involves actively attracting industrial relocation to Indonesia, strengthening domestic supply chains to reduce external dependencies, and enhancing the value-added of commodity-based products. Implementing adaptive investment policies and providing appropriate incentives can further solidify Indonesia's position as an attractive investment destination in the face of global uncertainty and supply

chain reconfigurations.

- **Enhancing the Quality of Democratic Institutions.** To ensure that democratic processes genuinely contribute positively to economic growth, policy efforts must shift focus from merely the formal aspects of democracy to a concerted improvement in the quality of governance. This encompasses strengthening the rule of law, significantly increasing transparency across all governmental operations, and systematically eradicating corruption at every level of administration, including provincial governance. Robust and corruption-free institutions are fundamental to fostering a more conducive business climate and enhancing investor confidence, thereby allowing democratic structures to effectively support economic development.
- **Maintaining Financial Sector Stability.** The Financial Services Authority (OJK) and Bank Indonesia (BI) must continue to reinforce their macroprudential frameworks and supervisory mechanisms to safeguard the health and integrity of the financial sector. While the current NPL levels do not pose a significant systemic threat, continuous and rigorous monitoring of bank asset quality and their intermediation capacity remains paramount. This vigilance is especially crucial to mitigate potential risks and ensure financial resilience in the event of unforeseen economic shocks.
- **Adaptive Inflation Management.** Monetary and fiscal policies should continue to be synergized to ensure careful and adaptive management of inflation.¹ While moderate inflation can be a healthy indicator of economic growth, uncontrolled price increases can severely erode public purchasing power and deter investment. It is imperative to proactively anticipate global commodity price shocks that could trigger domestic inflation and to implement responsive strategies aimed at stabilizing prices at both national and regional levels.
- **Strengthening Regional Economy.** Recognizing the inherent heterogeneity across Indonesia's provinces, economic development policies must be meticulously tailored to address the unique potential and specific challenges of each region. This includes actively promoting regional economic diversification, enhancing local competitiveness, and ensuring a more equitable distribution of growth benefits across all provinces to foster inclusive and sustainable development nationwide.

Declaration of AI and AI-assisted technologies in the writing process

During the preparation of this work, the author used **Gemini** in order to **search for the latest relevant journals**. After using this tool/service, the author reviewed and edited the content as needed and take full responsibility for the content of the publication.

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