Foreign Direct Investment and Economic Growth in ASEAN 5

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Foreign Direct Investment and Economic Growth in ASEAN 5

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Abstract

In ASEAN 5 countries namely Indonesia, Vietnam, Thailand, the Philippines and Malaysia have almost the same culture, in terms of social and economic aspects, the 5 countries have links between one country and another, so it is possible that the flow of foreign investment has a close relationship with economic growth. This study aims to determine the relationship between Foreign Direct Investment (FDI) and Economic Growth in ASEAN 5 Periods 1986-2017. This research is a two-way relationship research between the independent variable and the dependent variable that are reciprocal. The type of data used is the 1981-2017 time series data. Sources of data obtained from the World Bank. Data analysis technique uses Granger Causality analysis to see the 2-way relationship, and VAR (Vector Auto Regression) analysis by looking at the implus response factor for non-stationary data using VECM (Vector Error Correction Model) analysis. The results of the study state that based on the Granger Causality test there is no relationship between FDI and GDP and vice versa between GDP and FDI. Based on the VECM test there is a relationship between FDI and GDP.

Keywords: FDI, Economic Growth, VAR and VECM

INTRODUCTION

Economic growth is believed to be a measure of the success of a country, because it is a process of increasing output of goods and services that will increase national income. Economic growth is supported by an increase in various other variables such as investment and international trade.

The factors driving economic growth according to Todaro, 2003 are manifested in three main components, first, capital accumulation which includes all forms and types of new investments that are invested in land, physical equipment, and human capital. Second, population growth will further increase the number of the workforce. Thirdly technological advances which in the simplest sense occur because of the discovery of new ways or improvements to old ways. In this case investment is one of the drivers of economic growth, the statement is also supported by Lamsiraroj and Ulubasoglu, 2015 which shows there is a positive influence between FDI and economic growth in 140 countries in the period 1970-2009, the most powerful influence is in developing countries, whereas according to Almfraji and Almsafir, 2014 that in the long run there is a relationship between FDI and Economic Growth in the State of Qatar, in addition there is a positive effect of FDI on economic growth in the country of Qatar.

In essence, the average economic growth varies from country to country. In several Asian countries, such as China, Hong Kong, Singapore, South Korea, and Taiwan, the average real income of the population has increased by around 6% per year in the last fifty years, (Mankiw, 2014: 39). In countries that are members of ASEAN the rate of economic growth differs between countries even though they are almost culturally similar.

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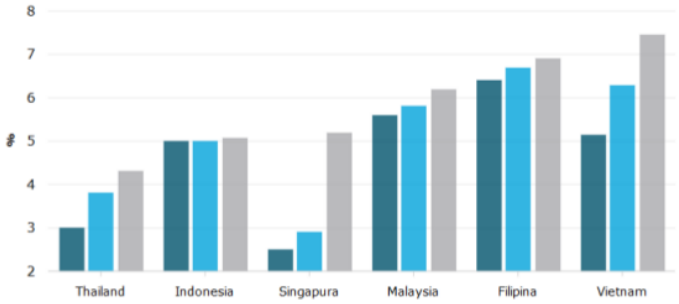

Figure 1.1. Economic Growth in 6 ASEAN Countries Quarter I-III 2017
Source: Tradingeconomics, 2017

A number of ASEAN countries experienced accelerated economic growth throughout 2017. In the third quarter the economies of Vietnam and the Philippines accelerated to beat China, but the Indonesian economy stagnated in the first, second and third quarters.

Vietnam's economic growth reached 7.46% in the third quarter, bigger in the first quarter and second quarter of 5.15% and 6.28%, compared to other ASEAN countries the highest economic growth in Vietnam, the condition is caused by the main export factors from industry foreign property.

Economic growth supported by investment is considered to increase the productivity of a country or region. Investment is the purchase of goods that will later be used to produce more goods and services (Mankiw, 2006: 12). FDI is also a supporter of a country's economic growth. There is granger causality between FDI and GDP (Tekin, 2012; Lamsiraroj and Ulubasoglu, 2015; Ibrahiem, 2015; Khatun and Ahamad, 2015; Khatun and Ahamad, 2015; Abdouli and Hammami, 2016).

Based on the introduction above, the formulation of the problem of this research is whether there is a relationship between Foreign Direct Investment (FDI) and Economic Growth (GDP) and vice versa whether there is a relationship between Economic Growth (GDP) and Foreign Direct Investment (FDI) in ASEAN 5 period 1981 -2017?

Based on the background and the formulation of the problem, the purpose of this study is to determine the relationship between variables FDI and Economic Growth and vice versa
The urgency of this research is to develop a new model related to the causality of the relationship between FDI and economic growth in ASEAN countries 5.

METHOD

This research is a two-way relationship between the independent variable and the dependent variable that are reciprocal, meaning that one variable can be the cause and also the effect on other variables, and vice versa.

The purpose of this research is explanatory research (explanatory research) where explanatory research is a type of research that explains the causal relationship between one variable with other variables through hypothesis testing.

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The object of this research is ASEAN 5 Countries, namely Indonesia, Malaysia, Thailand, Vietnam and the Philippines by looking at the relationship between Foreign Direct Investment and Economic Growth. The reason for choosing the object is because the characteristics and socio-cultural culture are almost the same, besides this there is a linkage of the economic sector between one country and another.

Data collection techniques use documentation studies by collecting secondary data, taking notes, and processing data related to this research. According to Azwar (2001: 91) Secondary data is usually in the form of documentation data or report data that has been available. The data used include: Foreign Direct Investment (FDI), exports, government spending and Economic Growth (GDP). While the type of data used is time series data in 1981-2017. Sources of data obtained from the World Bank.

The data analysis technique of this study used the VAR and VECM models. According to Greene, 2002 The shape of the VAR equation has changed a lot but not only has the shape of the equation changed, the variables in the equation have changed too, VAR has not only shaped a number of structural models but also aims to analyze and forecast macroeconomic activity and explore the effects of changes in policy and external stimulus on the economy. In addition to forecasting, VAR has been used for two main functions, testing Granger causality and studying the effects of policy through implus response factors and variance decomposition.

According to Gujarati (1995) there are several advantages of the VAR method including: (1) Simple method; no need to worry about determining which variables are endogenous and which are exogenous. All variables in VAR are endogenous. (2) Simple estimation; that is, the OLS method can be applied to each equation separately. (3) Forcasting with this method is in many cases better than several models of simultaneous equations.

Vector Error Correction Model (VECM) is the development of a VAR model for deeper analysis if we want to consider the existence of non-stationary data behavior (Ekananda, 2016).

The main differences in cointegration equations in VECM include: The resulting cointegration equation is a form of restriction from the VAR model, where the VAR model assumes that there are dynamic relationships of several interrelated variables (vectors). 2. The resulting cointegration equation is obtained from the johansen method, where cointegration results from the measurement of the eigenvalues of several variable combinations. 3. The composition of the cointegration equation is determined by the order of the variables in the VECM model. 4. Cointegration equation arrangement shows the relationship between equations and between variables simultaneously dynamically. 5. The composition of the cointegration equation shows the relationship between equations and between variables simultaneously dynamically. 6. The compilation of the cointegration equation must begin with the preparation of the VECM in accordance with economic theory at the beginning of the study. The cointegration equation that is formed is a consequence of the compilation of theories and VECM models that were prepared earlier (Ekananda, 2016).

RESULTS AND DISCUSSION

Economic growth in the five ASEAN countries has fluctuated. Since 1981-1996 the rate of economic growth in ASEAN 5 countries experienced positive growth, but since 1997-1998 in several ASEAN countries especially Indonesia, Malaysia, the Philippines, Thailand and Vietnam experienced negative economic growth, this is due to the financial crisis that occurred in some Asian countries, the financial crisis began in Thailand because of the fall in the value of the Bath

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currency which eventually impacted on several other Asian countries. The impact of the 1997-1998 economic crisis was most felt by the Indonesian state, this was seen in conditions of growth that dropped dramatically with a negative growth value compared to other ASEAN countries namely Malaysia, the Philippines, Thailand and Vietnam.

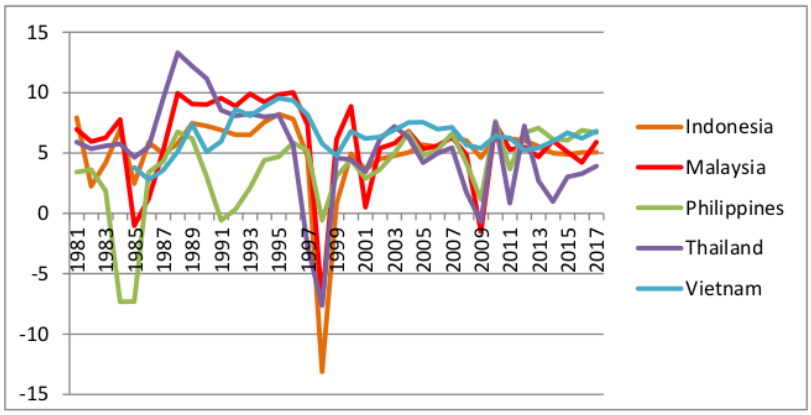

Figure 5.1 Economic Growth in ASEAN Countries 5
Source: World Bank, 2017

In 1999 economic growth showed a stable development compared to previous years, the movement of economic growth had grown positively in ASEAN 5 countries. However, economic growth weakened again after the global crisis in 2008. The global economic crisis that occurred in 2008 actually started in a crisis the United States economy which then spread to other countries around the world, including ASEAN countries such as Malaysia, Thailand, the Philippines, Vietnam and Indonesia. The global economic crisis in 2009 began in the United States due to the impetus for consumption (propincity to consume) . The American people live in consumerism outside the limits of the ability of the income it receives. They live in debt, shopping with a credit card, and housing loans. As a result, financial institutions that provide credit are bankrupt because of loss of liquidity, because the company's loans to housing creditors have been mortgaged to lending institutions. In the end, the companies must go bankrupt because they cannot pay all their debts which are due at the same time. The collapse of the financial companies resulted in the Wall Street stock market becoming powerless, large companies unable to survive. The 5 ASEAN countries that were most affected by the 2009 global economic crisis were Malaysia and Thailand. Until 2017 economic growth in ASEAN 5 countries experienced a positive growth rate despite fluctuating developments.

The development of foreign capital inflows in several ASEAN 5 countries is different, since 1981-1996 FDI conditions experienced rapid growth, especially in Vietnam and Malaysia, as we know Vietnam is a communist country that is most targeted by several foreign investors, besides because of the success stories of giant shoe companies such as adidas and nike, Vietnam is also famous for its high technology proven that Intel has been investing in the country since 2010, followed by LG Group and Samsung, which are reaping successful investing in Vietnam.

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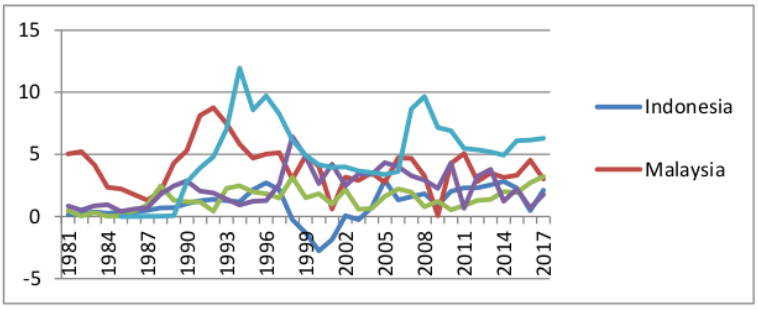

Figure 5.2 Foreign Direct Investment in ASEAN Countries 5

Source: World Bank, 2017

The growth of FDI that is most concerned about the Indonesian state in 1997-1998, the impact of the monetary crisis is strongly felt in Indonesia this is characterized by the weakening of the rupiah against the US dollar which led to Indonesia's rich people, both native and ethnic Chinese officials, since then get ready to save his assets abroad to anticipate domestic political instability. Since the beginning of December 1997 until the beginning of May 1998 there has been a massive capital flight out of the country due to political instability such as the issue of the President's illness and elections (World Bank, 1998: 1.4, 1.10).

Trade openness is one measure of a country's readiness to establish product specialization in the field of trade, according to the trading theory of Adam Smith and David Ricardo, each country has comparative advantages and advantages so that each country will certainly specialize.
Figure 5.3 below shows that Vietnam and Malaysia have a high value of trade openness compared to other ASEAN 5 countries. Aside from the two countries being the destination of foreign investors, the country is a country with faster economic growth.

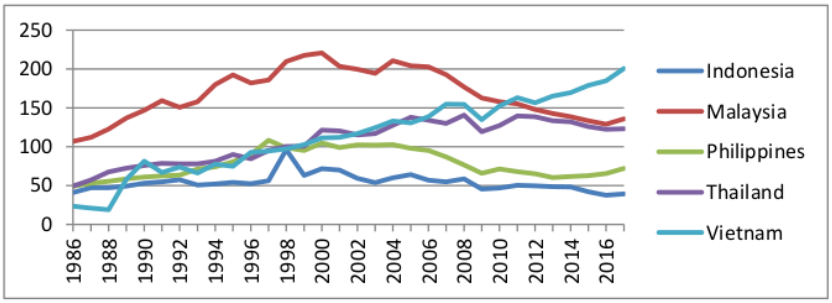

Figure 5.3 Trade Openness in ASEAN Countries 5

Source: World Bank, 2017

Based on the estimated results of the chow test from Table 5.4 shows that the Chi-Square probability value (0.4457) is greater than the critical probability (α = 5% or 0.05). This means that the null hypothesis (H0) is accepted and H1 is rejected. Thus it is known that the model is not good and not appropriate to use the Fixed Effect model panel regression analysis. Testing the determination of the best model is continued by using the Hausman Test.

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Table 5.1 PLS, FEM and REM Model Testing Results

Variabel	*Panel Least Square*	*Fixed Effect Model*	*Random Effect Model*
Trade	-0.018870	-0.027422	-0.018870
	(0.0070)*	(0.0417) *	(0.0072)*
FDI	1.059017	0.998433	1.059017
	(0.0005)*	(0.0000)*	(0.0000)*
Adjusted R-square	0.227080	0.223281	0.227080
F-*statistic*	0.000002	0.000018	0.000002
Uji Chow	1.616356		
Prob.	0.4457		
Uji Hausman	1.545142		
Prob	0.4618		
LM	29.14296		
Prob.	0.0000*		

Source: Results of Eviews 7

Based on the thirsty test in table 5.1 it is known that the Chi-Square probability value (0.4618) is greater than the critical probability (α = 5% or 0.05). This means that the null hypothesis (H0) is accepted and H1 is rejected. Thus it is known that the model is not good and not right to use panel analysis of random effects regression models. Testing the determination of the best model is continued by using the LM Test.

Based on the LM test in table 5.1 it is known that the Chi-Square probability (0,000) is smaller than the critical probability (α = 5% or 0.05). This means that the null hypothesis (H0) is rejected and H1 is accepted. Thus it is known that the model has been good and appropriate using random effects model panel regression analysis.

Stationarity test is used to see whether the research variable has a unit root or does not have a unit root. Stationary data is not found unit roots while non stationary data has unit roots. Unit root testing uses Augmented dickey fuller test, stationary data must have a t-statistic value at the ADF greater than critical values.
Based on the unit root test results in table 5.2 below shows that the GDP, FDI and TRADE variables in the study are not stationary on the data level, the probability value is still greater than the critical value α = 0.05. The output results indicate that the data is not stationary at the data level level.

Table 5.2. Unit Root Test Results

Levin, Lin, Chu (LLC)			
Tingkat	GDP	TRADE	FDI
Level	0.0002*	0.1002	0.2628
1st *Difference*	0.0007*	0.0071*	0.0000*
2nd *Difference*	0.0000*	0.0000*	0.0000*
Im Pesaran, Shin (IPS)			
Tingkat	GDP	TRADE	FDI
Level	0.0002*	0.7722	0.743
1st *Difference*	0.0000*	0.0000*	0.0000*
2nd *Difference*	0.0000*	0.0000*	0.0000*
Fisher- *Augment Dickey Fuller* (F-ADF)			
Tingkat	GDP	TRADE	FDI
Level	0.0008*	0.8715	0.1033
1st *Difference*	0.0000*	0.0000*	0.0000*

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2nd *Difference*	0.0000*	0.0000*	0.0000*
Fisher- Phillip Perron (Fisher-PP)			
Tingkat	GDP	TRADE	FDI
Level	0.0001*	0.5094	0.0417
1st *Difference*	0.0000*	0.0000*	0.0000*
2nd *Difference*	0.0000*	0.0000*	0.0000*

Source: Results of Eviews 7

While based on unit root test results using the first difference data, it can be seen that the GDP, FDI and TRADE variables in the study have been stationary because the probability value is smaller than the critical value α = 0.05 each 0.0000> 0.05. The output results indicate that the data is stationary.

To see the research data, there is cointegration or not by using the Johansen Cointegration Test. The following is the Johansen Cointegration Test Results using lag length 1 with fist difference data. If the Trance Statistics value is greater than the Critical Value then the equation is cointegrated and vice versa if the Trance Statistics value is smaller than the Critical Value then the equation is not cointegrated, or the ADF probability value> 5% critical value, in the VAR model the equation used is the equation used not cointegrated.

Table 5.3. Cointegration Test Results

Prob. ADF	Keterangan
0.0001	Terkointegrasi

Source: Processed Eviews 7

The Johansen Cointegration Test results in Table 5.3 above show the cointegration equation with the ADF Probability value is smaller than the Critical Value (0,0001 <0.05), so in this study using the Vector Error Correction Model (VECM).

To determine the optimal lag length using the Akaike Information Criterion (AIC) criterion value. The smallest AIC value used in determining the optimal lag. Based on Table 5.4 below it appears that the smallest Akaike Information Criterion (AIC) value is located at lag 2, then the optimal lag length is 2 with an AIC value of 15,62982.

Table 5.4. Optimal Lag Length Determination Results

Lag	AIC
0	19.38927
1	15.63257
2	15.6298*
3	15.71951
4	15.89785
5	16.02985
6	16.13867
7	16.17018
8	16.29902

Source: Result Of Eviews 7

Based on the Granger Causality test results in table 5.5 below shows the probability value is greater than sig 0.005 both GDP, FDI and TRADE variables, meaning that there is no two-way relationship

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between GDP against FDI and vice versa, there is no two-way relationship between TRADE to FDI and vice versa, and there is no two-way TRADE relationship to GDP and vice versa.

Table 5.5. Granger Causality Test Results

Null Hypothesis:	Obs	F-Statistic	Prob.
GDP does not Granger Cause FDI	90	1.54031	0.2202
FDI does not Granger Cause GDP		0.51103	0.6017
TRADE does not Granger Cause FDI	90	1.92462	0.1522
FDI does not Granger Cause TRADE		3.07619	0.0513
TRADE does not Granger Cause GDP	90	0.30541	0.7376
GDP does not Granger Cause TRADE		2.86166	0.0627

Source: Results of Eviews 7

Because with the Granger Causality test there is no relationship between FDI and GDP and vice versa, the estimation is continued using the VECM method to see the long-term relationship between FDI and GDP, TRADE and GDP.

VECM estimates are used to look at past FDI, GDP and TRADE movements, in addition, the VAR and VECM models are not only structural but aim to analyze and forecast macroeconomic activity and explore the effects of changes in policy and external stimulus on the economy. Cointegration test results above that each variable is cointegrated, the model used is the VECM model.

Implied Response Factor (IRF)
Furthermore, to find out the shock (shaking) of each variable against other variables using the Response Response Factor (IRF). The figure below shows the period in which one period represents one month. This study uses a period of 24 months, so that the period used in the IRF test is 24 periods. The following is the result of IRF estimation based on the relationship of each variable (See Figure 5.6)

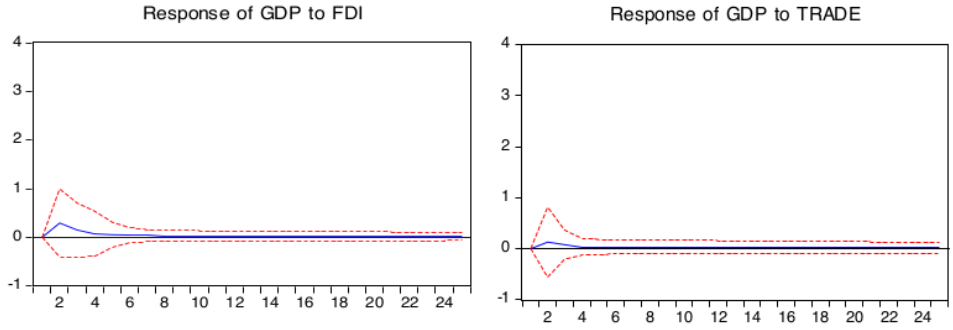

Figure 5.6. Implied Response Factor (IRF) Results

In the estimation of the impulse response above, the GDP response to the shock variable FDI shows that the GDP response to FDI is fluctuating. In the first period to the second period, it was seen that the GDP variable gave a positive response to FDI of 0.2%. In the next period, the GDP response to FDI shock began to decline but did not reach the negative direction to the range of 0.02%. The response will reach a balance point in the 8th period until the 22nd period with a response of 0.001%. This indicates that in the long run there is a positive relationship between GDP and FDI.

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Whereas based on the results of impulse response the GDP response to TRADE shock shows that the GDP response to TRADE shock was positive and increased in the second period which was 0.1%, but in the next period the GDP response to TRADE began to decrease to around 0.001% in the 3rd period until it reached balance in the 4th to the 24th periods. This indicates that in the long run there is a positive relationship between GDP and TRADE.

Variance Decomposition (VD)

Analysis of Variance Decomposition (VD) is an analysis to predict the contribution of variable variance due to changes in certain variables in the VAR model. With this analysis it will be known how much the contribution of the FDI variable is due to changes in the GDP variable in each period and how much the contribution of the GDP variable due to changes in the variable FDI in each - each period and how many contributions the GDP variable is due to changes in the TRADE variable. VD test is needed to test the estimated error variance of a variable that is how big the variance before and after shock, both shock originating from oneself and from other variables.

Table 5.6. Output Variance Decomposition (DC) Results Of FDI, GDP and Trade

Period	S.E.	GDP	FDI	TRADE
1	3.379452	100	0	0
2	3.545851	99.54319	0.418096	0.038712
3	3.579488	97.68603	0.59725	1.716723
4	3.613679	97.28397	0.602202	2.113825
5	3.621565	96.98103	0.825978	2.192987
6	3.624868	96.85161	0.82853	2.319863
7	3.626995	96.84762	0.832439	2.319943
8	3.627606	96.82782	0.849818	2.322359
9	3.628028	96.80789	0.849762	2.342345
10	3.628233	96.80244	0.852318	2.34524
11	3.62848	96.79078	0.857015	2.3522
12	3.62872	96.77853	0.859404	2.362071
13	3.628946	96.76863	0.862947	2.368421
14	3.629187	96.75778	0.866858	2.375358
15	3.629428	96.7468	0.87026	2.382937

Source: Result Of Eviews 7

Based on the results of Variance Decomposition above, the biggest contribution lies in the GDP variable. The contribution of the GDP variable continued to decline until the 15th period but remained positive and was the most dominant among the other variables. In the third period the contribution of GDP has decreased from 99.54% to 97.68%, although the downward trend in the contribution of GDP until the 15th period remains positive and the most dominant among the other variables, up to the 15th period the contribution of GDP amounted to 96.74%

The second biggest contribution in influencing economic growth is the TRADE variable, the variance on the TRADE variable continues to increase until the end of the period, the highest increase lies at the end of the 15th period of 2.38%.

The contribution of variance to the FDI variable in influencing economic growth also experienced a positive trend, starting from the beginning of the period until the end of the period, this is indicated

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by the value of the initial variance of the second period of 0.41%, increasing until the end of the period of 0.87%.

Based on the Granger Causality test results, there is no 2-way relationship between FDI and GDP, according to the research of Dritsaki and Stiakakis (2014), Temiz and Gokmen (2014). There is no relationship between FDI and economic growth in 5 ASEAN countries (Indonesia, Malaysia, the Philippines, Thailand and Vietnam) due to the Granger Causality test to see a 2-way relationship between FDI and GDP and vice versa then the estimation is continued using the VECM method to see the long-term relationship between FDI and GDP, TRADE and GDP.

Based on the results of the VECM estimation shows the response of GDP to shock FDI gives a positive response and increases in the second period and the subsequent period has decreased and tends to be stable until the end of the 24th period. This indicates in the long run there is a positive relationship between GDP and FDI, in accordance with Tekin research, 2012; Lamsiraroj and Ulubasoglu, 2015; Ibrahiem, 2015; Khatun and Ahamad, 2015; Abdouli and Hammami, 2016, De Mello (1999); Sunde, 2017; Abbes, et al, 2015; Diby, 2014 and Nistor, 2014

Abdouli and Hammami, 2016 explained that international capital flows that entered the country, especially developing countries as host countries, were able to bring many positive effects both financial and non-financial. Aside from being a complement to domestic investment, for host country FDI will bring other positive influences such as accelerating the transmission of modern technology and developing human capital so that the level of domestic productivity increases and people's needs can be met, it will clearly increase economic growth in terms of GDP.

When viewed from the characteristics of the 5 ASEAN countries namely Indonesia, Malaysia, Thailand, Vietnam and the Philippines, the 5 ASEAN countries have almost the same characteristics, namely both developing countries with the main base of the agricultural sector, ASEAN 5 countries also have an open economy . In accordance with IRF results when there is a shock from direct FDI responds to changes in economic growth. this is certainly in accordance with the opinions of Dornbusch, Fisher and Strartz: 2004 which states economic growth is related to growth in inputs such as labor and capital, and improvements in technology, Dornbusch, Fisher and Strartz (2004) also argue that if FDI rises then it will respond quickly by economic growth, this has happened in the 5 ASEAN countries, the ups and downs of FDI always bring changes to economic growth.
Whereas based on the results of impulse response the GDP response to TRADE shock shows that the GDP response to TRADE shock was positive and increased in the second period but in the next period the GDP response to TRADE began to decline until the 3rd period until it reached a balance in the 4th period to the 24th period , this indicates that every increase / decrease in GDP will be responded to with an increase / decrease in TRADE and vice versa every increase / decrease in TRADE will be responded to by an increase / decrease in GDP, this is in accordance with the research of Belloumi (2014).

Hoang (2012) argues that with a high trade openness, which causes the trade barrier to decline this is an opportunity for foreign investors to be able to take advantage of the comparative advantage of the host country to be able to reexport so that it will increase economic growth in terms of GDP.

In developing countries, especially ASEAN 5 (Indonesia, Vietnam, Malaysia, Thailand and the Philippines) is unique in product diversification. The basis of the agricultural sector has always been an advantage, especially in Indonesia, Vietnam and Thailand, by implementing high trade

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openness that will cause openness with several other countries so that product specialization can occur.

The high trade openness policy in ASEAN 5 countries is very conducive to increasing international trade transactions both through the imposition of tariffs and quotas. Thus the government policy to implement various international trade policies aimed at increasing the value of trade openness by opening the widest possible space for trade traffic between countries is the right step for ASEAN countries to do. This is important because trade openness has an impact which is very large towards efforts to increase economic growth better and faster. The existence of export and import policies with a new and productive system is very possible by the governments of ASEAN countries to spur economic growth and catch up with the developed countries. And the socialization of government regulations in the field of trade between countries needs to be done, in which the community/ international trade actors to fully understand the regulations issued by the government. This condition enables business actors to determine the appropriate business sectors to be carried out so that long-term trade openness can continue to drive economic growth.

CONCLUSION

Based on the Granger Causality test there is no relationship between FDI and GDP and vice versa between GDP and FDI, there is no relationship between trade openness to GDP and vice versa between GDP and trade openness. Based on the VECM test there is a relationship between FDI to GDP and trade options to GDP

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