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Investment influence on east java economic growth

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Abstract

This study aims to examine and analyze the effect of investment in the manufacturing industry sector on the economic growth of East Java, Indonesia. The research period is five years, starting from 2004 / 2018. This paper uses the method of multiple linear regression analysis with the findings that explain that foreign investment (PMA) has a positive and significant effect on economic growth. This finding is in line with the reality on the ground that the number of foreign investors who invested in East Java is quite large and the sector that is mostly interested is the food industry sector (culinary). While domestic investment (PMDN) has no significant effect on growth. This condition was influenced by several factors including: 1) Risk Country; 2) low coordination between institutions and; 3) low financial sector connectivity. While efforts to increase investment, can be done through programs of reform, deregulation, and bureaucratization in all aspects of economic development.

Key words: Economic growth; investment; foreign investment; East Java

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INTRODUCTION

The flow of economic liberalization and globalization as a consequence of the agreement on General Agreement on Tariff and Trade (GATT) and the World Trade Organization (WTO) supported by technological changes in each country are globally influential. Liberalization forces every State to open up all protection and international investment for the domestic economy. With that condition, the most important thing for the country's economy to increase economic growth is to look at the value of investment, creates new jobs, and alleviates poverty (Mankiw 2006). In neo-classical theory, a country needed to establish an accumulation of capital (Kuncoro 2014). Foreign investment acts as a transfer medium for resource needs such as technology, managerial capabilities, and export channels (Kobrin, 1997 in (Sudarsono dan Suryanto 2017)). Empirical studies in general provide an indication that the flow of foreign capital the positive impact of economic growth on developing countries in the Asian-African region ((Sodik dan Nuryadin 2005). The country's economic growth is based on the industrial sector with a contribution of 19.82 per cent in 2018. The dynamics of the industrial sector in general move in line with economic growth (Liu dan Yeung 2008).

Manufacturing industry in East Java is one of the mainstay sectors in driving economic growth with proven contribution to GDP reaching 19.82 percent in 2018. Not only does the national industry face a big problem behind the beauty of industrialization, namely the shallow industrial structure problem and the high import content of raw materials in the industrial sector (Sardjono 2009). Various efforts have been made by the government, one of which is through the XVI Economic Policy Package, namely: (a) Tax Holiyday; (b) Relaxation of negative investment lists; and (c) Increase in foreign exchange proceeds from exports.

Efforts to strengthen national industry, conducted by the government through the PP 29 of 2018 concerning national industrial empowerment. This government regulation states that the load of raw materials in the production process must be 70 percent domestic and 30 percent imported. This arrangement seeks to direct the behavior of industrial companies in their production processes to prioritize the use of raw materials from within the country so as to enable an increase in value added to domestic production.

East Java itself consists of several large islands with different economic growth rates. One of them is East Java Province which has a considerable role in the national economy with a contribution of 14.67 percent to the National GDP and 29.73 percent is a contribution from the manufacturing industry sector to Gross Domestic Product og east java.

The manufacturing industry in east java can be competitive (Handoyo 2016). explained that manufacturing industries that have high local and international competitiveness are the paper industry and the wood industry. In contrast, industries that have low local competitiveness or competitive advantage are food, beverage, and food processing industries. The strategy for developing the East Java manufacturing industry is not only aimed at increasing comparative advantage but also for increasing competitive advantage through increasing the efficiency of the production process (Azhar dan Arifin 2011).

The large potential of the East Java manufacturing industry sector is relatively increasing. Manufacturing industry ratio index in PDRB of East Java is also called the industrialization ratio, showing an increasing trend. The increase in the industrialization ratio is a very favorable economic condition for the economic development of East Java in the long term, considering that input resources such as the natural resource potential of East Java are very large (Istifadah 2014), and (Kurniasari 2016). Research want to know factor on the economy and industries in east java. This research determine the effect on investment in sector industry manufacturing on East Java's economic growth.

Literature Review

Industry

Industry is a procesinf activity raw materials in to finished goods (Hannah dan Kay 1977). Law No.5 of 1984, defines industry as an economic activity that processes raw materials, semi-finished goods, and / or finished goods into goods which have a higher value in their use. According to (Arsyad 2014). National industry is divided into 3 groups: 1) Basic industry; 2) Small industries; and 3) Downstream industry.

Manufacturing Industry

Industry or manufacturing industry is a processing the comes from the industry business fields in calculating derived from the calculation of national income with a production approach (Hastina, 2007 in (Napitupulu dan Hati 2018)). According to the statistics center (BPS) is a manufacturing industry is an economic activity changes basic goods mechanically and chemically (consumer).

Classification of Manufacturing Industry

The manufacturing industry is a broad economic activity, the number and type of industries vary by country. International Standard of Industrial Classification (ISIC) classified manufacturing industries into nine groups based on the approach of commodity groups, namely (dumairy, 1996 in (Suprapto 2011)): food and beverage industry, tobacco industry, textile industry, textile industry, apparel and leather industry, wood and wood products industry and paper industry, chemical industry and chemical goods; non-metal excavation industry, except oil and coal; base metal industry; metal industry, machinery and equipment and other processing industries. Meanwhile, based on the statistical center (BPS) classified manufacturing industries into four groups based on the number of workers in large industries with a workforce of> 100; medium industry with a total workforce of 20-29; small industries with a workforce of 5–19; and home industry with a workforce of 1-4.

Industrialization Strategy

History records the diversity of policy strategies adopted by each country. According to (Kuncoro 2007), there are those who try to spur development with trade expansion. There are also those who implement import substitution strategies. Outward Looking policies are identical to free trade through export promotion policies. Meanwhile for the policy of looking inside is (Inward Looking) protectionist policy and emphasizes more on import substitution (Kuncoro 2007).

Investation

By definition, investment is investment expenditure or shopping or a company to buy capital goods and equipment to increase the ability to produce goods and services available in the economy (Ghonio dan Sukirno 2017). According to Todaro (2000), investment plays an important role in moving the economic life of a country. So that investment demand must be increased through technological innovation (Mankiw, 2003).

Research on investment with economic growth has been carried out, including: (Rustiono 2008); and (Sodik dan Nuryadin 2005) explain that economic growth is largely determined by investment and its influence is significant. This explains that high investment will automatically increase economic growth and increase employment.

Domestic Investment (PMDN)

Based on law number 6 article 1 of 1968, domestic investment is part of the wealth of the East Java community both directly and indirectly including rights and objects owned by the state and private national or foreign private domiciled in Java East. In addition, domestic investment can be interpreted as a user of wealth that can be carried out directly by the owner himself or indirectly, through the purchase of bonds, stocks, deposits, and savings of at least 1 year.

Foreign Investment (PMA)

Foreign investment (PMA) is an investment activity carried out by foreign capital owners in the country to get an advantage from the business done. According to him, the inclusion of foreign capital is needed to accelerate economic development. Whereas according to law number 1 of 1967 and number 11 of 1970 concerning foreign investment and credit, including: 1) foreign payment instruments that are not part of East Java's foreign exchange assets, which with government approval are used to finance companies in Indonesia; 2) tools for the company, including new discoveries owned by foreigners and materials imported from abroad into the Indonesian territory; and 3) part of the company's proceeds based on this law are permitted to be transferred, but are used to finance companies in East Java.

Economic growth

Growth of Harrord-Domar

According to Harrord-Domar's theory, capital is an important factor that determines economic growth (Sutawijaya 2010). The formation of capital can be obtained through the process of accumulating savings. This theory explains that the increase in production capacity and national income is determined by the increase in public expenditure. Thus, even though production capacity increases, new National income will increase only if there is an increase in public expenditure (Kuncoro 2014).

Solow-Swan Economic Growth

The Solow growth model is designed to show how the growth of the capital stock, labor force growth, and technological advances interact in the economy, as well as how it affects the output of goods and services as a whole country (Mankiw 2006) in (Ernita et al. 2013) . According to (Arsyad 2014), in the Solow-Swan theory, the capital output ratio (COR) has a dynamic nature.

Growth of the Caldorian Industry

Kaldor's theory considers that the manufacturing industry sector is a growth engine for a region in increasing the growth of other sectors and at the same time increasing economic growth. Furthermore, the theory of Caldor states that Increasing Return To Scale can only be created with the accumulation of capital and technological progress. (Sholihah et al. 2017) in his research stated that GDP growth, labor productivity in the manufacturing sector, and the growth of the non-manufacturing sector have a positive relationship with the growth of the manufacturing industry sector.

Inclusive growth

The theory of inclusive growth is used as a frame of mind to identify growth inhibitors in terms of providing employment derived from investment formation (Nengsih 2015). This growth diagnosis works by analyzing the most influential components of growth and finding out what factors can affect these components. According to (Dzialek 2009), the component that inhibits growth in a region is the investment climate and what factors will affect the level of investment.

Investment Relations to Economic Growth

According to Boediono (1992) Investment is expenditure by the producer sector (private) in purchasing goods and services to increase the stock used. (HABIBI 2016), Dorbusch & Fischer argues that investment is the demand for goods and services to create or increase production capacity in the future. Whereas, Todaro (1981) general conditions development a country are (Rustiono 2008): 1) Capital accumulation; 2) Development of the population coupled with labor and expertise; and 3) technological progress. Furthermore, (Sjafii 2009) explains that investment activities can increase economic activity, increase employment opportunities increase national income and in turn increase the level of prosperity of the community.

Trade Concept

The model used in this study is Gravity Model. In the context of trading this model states that the intensity of trade between countries will be positively related to the national income of each country and is inversely related to the distance between the two. In other words, (Lewis 2013) the Gravity Model can explain international trade flows well, where bilateral trade flows are linear log functions of income and distance. Theory from Helpman and Krugman in (Millimet dan Osang 2007) explains that similarities in the size of the economy have a positive influence on trade, a country that is almost the same size as its economy will do more trade. Furthermore, trade flow policies are divided into two types, including:

Tariff Policy (Tariff Barrier)

The historical trade barriers are tariffs. Tariff is a tax imposed on goods traded cross-territorial. Judging from the origin of the commodity there are two types of tariffs, namely, export tariffs (Export Tariff) and import tariffs (Import Tariff). The tariff applied to imported goods aims to be able to increase domestic prices, imported goods can make domestic products compete.

Non-Tariff Policy (Non Tariff Barrier)

Non Tariff Barrier is a trade policy other than import duty which can cause distortion, thereby reducing the potential benefits of international trade (Hady, 2004 in (Malik dan Wulandari 2006)). In general, Non Tariff Barrier can be divided into three types, namely: a) Specific Limitation (Specific Limition); b) Customs Rules; and c) Mix of government hands (Government Participation).

METHOD

Research Approach

The approach used in this study is a quantitative approach in the hypothesis, analysis of data and conclusions with aspects of measurement, calculation and certainty of numerical data (Musianto 2004). The purpose of this approach is more to the results of research in the form of generalized conclusions and measurable explanations of phenomena. While the type of data used is secondary data in the form of time series data from 2004 to 2018 in East Java.

Operational definition

Economic growth

Economist growth is defined as an increase in GDP or GNP. So economic growth measures the achievement of the development of an economy in East Java. the data used in this study is data on East Java economic growth.

Foreign investment (PMA)

Investments made by foreign investors in various fields, especially in the manufacturing industry, the data used in this study are data on foreign investment in East Java.

Domestic Investment (PMDN)

Investments made by domestic investors in various fields, especially in the manufacturing industry, the data used in this study are data on domestic investment in East Java.

Analysis Model

This study uses a model of multiple regression analysis (Multipler Regression). The model used can be formulated as follows, namely:

$$\mathbf{PEi = \beta0 + \beta1PMDN + \beta2PMA + \beta\varepsilon}$$

Where:
PEi = East Java Economic Growth (Percent)
PMDN = Domestic Investment in East Java (Rupiah)
PMA = Foreign Investment in East Java (Rupiah)

DISCUSSION

Investment Structure

Based on the investment value of all economic sectors in East Java in 2017 amounting to IDR 66.53 trillion, which consisted of foreign investment of IDR 21.49 trillion and domestic investment of IDR 45.04 trillion. The largest investment is owned by the building sector, which is 1.14 trillion, the high investment in this sector is because East Java has a high value of building projects. Investment in the processing industry sector in East Java in 2017 is IDR 23 trillion or 15.45 percent of the total investment in the economy sector as a whole and ranks second from all economic sectors in East Java. The investment value consists of the formation of fixed capital of Rp 18 trillion or 13.49 percent of the total fixed capital formation. The high investment in this sector is due to the high level of human resources in this sector, infrastructure that is sufficient to support economic activities.

Investment in the Industrial Sector

Table 1.1 shows the large realization on foreign investment investments in the industrial sector in East Java in 2017, the industrial sector that receives the largest FDI investment is the food industry, which is Rp 6.92 Trillion, then second in the Metal industry sector. machinery & electronics Rp. 3.06 Trillion. Furthermore, other industrial sectors and the Chemical & pharmaceutical industry amounted to Rp. 2.41 and 2.32 Trillion. Whereas the Minerals and metals Industry and the Rubber & Plastics Industry have a very small value of FDI investment realization, which is only Rp. 0.78 and 0.92 Trillion. From the results that foreign investment is greater ini value than domestic investment in investment opportunities East Java. Large diversity of food in East Java has made foreign investors interested in investing in the food industry sector.

Table 1.
Realization of FDI in the Industrial Sector in East Java in 2017

Sector	Investment (Rp. Triliun)
Food Fucturing Industry	6,92
Metal, machinery & electronics industry	3,06
Chemical & pharmaceutical industry	2,32
Rubber & plastic industry	0,92
Mineral and metal industry	0,78
Other industries	2,41

In table 1 shows the realization of domestic investment investment in the industrial sector in 2017, it can be seen that the food industry sector has the highest value of realization of domestic investment, which is worth 7.95 trillion, indicating that the interest of foreign investors in investing in this sector very large. The second position is the Mineral and metal industry with an investment realization value of Rp. 3.38 Trillion. Next, the industrial sector is Rp. 3.05 Trillion. While the industrial sector which has the lowest FDI realization is the Paper & Printing Industry sector with a value of 1.15 Trillion. Although the value of domestic investment also looks high, investors who are interested in investing are foreign investors who have more interest in investing in East Java.

Table 2.
Realization of Domestic Investment in the Industrial Sector in East Java in 2017

Sector	Investment (Rp. Trillion)
Food industry	7,95
Metal, machinery & electronics industry	2,70
Chemical & pharmaceutical industry	3,05
Paper & printing industry	1,15
Mineral and metal industry	3,38

The Role of the Industrial Sector Against Absorption of Labor

When viewed from the large number of workers, the industrial sector is a sector that absorbs the largest workforce and subsequently the trade sector. Due to the fact that the industrial sector is engaged in production so that it requires sufficient workforce in its business, the largest business sector is other industries namely absorbing employment of 44,625 people in 2017, food industry at 40,447 people and Metal, machinery & electronics industry at 11,082 people. While the industrial sector that absorbs the lowest labor force is the chemical & pharmaceutical industry which is equal to 5,838 people.

Tabel 3.
2017 East Java Industrial Sector Employment Absorption

Sector	Company	Labor
Food industry	852	40,447
Metal, machinery & electronics industry	455	13,999
Chemical & pharmaceutical industry	441	5,838
Rubber & plastic industry	96	6,274
Nonmetallic Mineral Industry	187	11,082
Other industries	809,41	44,625
Transportation, warehouse & communication	99	5,827
Trade & repair	517	6,233

If the government wants to reduce unemployment, then the sector that absorbs a lot of labor should be given an investment so that it can reduce unemployment. Labor Absorption in the Industrial Sector, shows that the sub-sector of the manufacturing industry which plays the greatest role in employment is other industrial sectors with the growth trend of employment in the sector always experiencing an increase every year. The sector that absorbs the lowest labor compared to other sectors is the industrial sector of transportation, warehousing & communication, the low absorption of labor because in the industry more technology is used so that less human labor is needed.

The Role of the Industrial Sector Against the Establishment of East Java GRDP

The contribution of seventeen sectors forming the East Java GRDP structure over the past 4 years reflected in the GRDP according to the business field did not show a significant change. The three dominant business fields that contribute to East Java GRDP are the manufacturing sector, trade sector, repair service sector, forestry and fisheries. The contribution of the three sectors in 2017 was 29.03%, 18.18%, 12.80%, and the total contribution of the three was 60.01%.

Table 4.
The Biggest Contribution of Three Sectors in East Java GRDP 2014-2017

Sector	2014	2015	2016	2017
Agriculture	13,56	13,65	13,43	12,80
Processing industry	28,95	29,31	28,88	29,03
Trade	17,34	17,60	17,98	18,18

The manufacturing sector has a very large role in the formation of East Java GRDP. Its contribution is stable, this can be seen from the percentage which from year to year tends to increase. These developments indicate that the manufacturing industry sector is able to contribute to the dominant value added and has grown rapidly beyond the growth rate of the trade sector and the agricultural sector.

Analysis Results

In the results of the regression analysis that has been done this research is to find out how the influence of domestic investment (PMDN) and foreign investment (PMA) on economic growth in East Java, where regression estimation results are obtained as follows:

Economic growth = 7,079 + 3,481PMA+ 5,436PMDN

The influence of PMDN and PMA variables on economic growth is shown in the following table:

Table 5.
Results of Regression Relations

R	0,642
R2	0,585
Adjusted R Square	0,521
Std. Error of the estimate	5,70871
Fsig.	3,907

From the table it can be seen that the value of R obtained is equal to 0.642 or equal to 64.2%. So that it can be said that PMDN and PMA in this study have an influence on economic growth in East Java but the influence given is said to be large.

Table 6.
Regression Results

Mod	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constanta)	7,079	,428		24,026	,000
PMA	3,481	4,588	,473	2,627	,005
PMDN	5,436	4,767	,345	1,096	,323

From the estimation results explain that the significant value of Foreign Investment is 0.005 less than 0.05. This illustrates that H0 is rejected, which means that Foreign Investment individually has a significant effect on East Java's economic growth. With the influence of foreign investment, it is expected that the greater the employment opportunities that occur in East Java so that it will open up more employment opportunities for human resources or workers in East Java. From the results of data processing shows that the significant value of Domestic Investment is 0.323 greater than 0.05, this explains that H0 is accepted which means that Domestic Investment individually does not have a significant effect on East Java economic growth. With results that are different from the value of foreign investments that have an influence on economic growth, the results of domestic investment show the results where the investment has no influence on economic growth. It can be seen that there is still a lack of facilities provided by the government to support the operation of the domestic market which is widely available in the East Java region. In addition, existing labor or human resources have not yet had the soft skills expected by investors.

The Effect of Foreign Investment (PMA) on Economic Growth in East Java

Foreign investment can be utilized by developing countries in spurring an increase in economic growth, to maintain and maintain a higher growth rate with substantial changes and reforms in the production structure and in mobilizing structural transformal funding sources.

Foreign investment can fill the gap between inventory savings, foreign exchange reserves, government revenues, and managerial expertise in the recipient country with the level of inventory needed to achieve growth targets and economic development. Thus, incoming foreign investment will encourage economic growth. The greater the foreign capital that enters, the higher the economic growth.

Based on the estimation results, the Regression Analysis concluded that foreign investment had a significant effect on economic growth in East Java with a value of 0.005 less than 0.05. These findings are in line with the research conducted (Wahyudi, 2005 in Salebu 2014); (Salebu 2014); dan (Bimantoro 2016) about the effect of foreign investment on economic growth, explaining that there is a positive relationship between foreign investment and economic growth.

Effects of Domestic Investment (PMDN) on East Java Economic Growth

Domestic Investment (PMDN) can be interpreted as spending or spending on investment or companies to buy manufactured goods, to increase the ability to produce goods and services available in the economy that come from domestic investment. Investment collects accumulated capital by building a number of buildings and equipment that are useful for productive activities, so the potential output of a nation will increase and long-term economic growth will also increase. It is clear that investment in particular Domestic Investment (PMDN) plays an important role in determining the amount of output and income. Economic influences that determine investment include investment costs determined by interest rates and policies (Samuelson dan Nordhaus, 1993 in (Hismendi dan Musnadi 2013)). Domestic investment has an influence on economic growth.

However, based on the estimation results of the Regression Analysis in East Java, it was concluded that domestic investment have not a significant effect on East Java's economic growth with a significant value of 0.323 greater than 0.05. These findings are in line with the results of the study (Apriansyah dan Bachri 2006) about Analysis of Causality Relationship Between Investments (Government, Foreign Private and Domestic Private) With Indonesian Economic Growth in the 1970-2005 period with the Vector Auto Regression model. Based on the causality test that significantly there is no causal relationship between government investment and economic growth, economic growth significantly influences foreign investment while foreign investment does not have a significant influence an Indonesia's economic growth, there is no significant influence among them domestic private investment and economic growth, economic growth has not been able to encourage and enhance economic growth.

CONCLUSION

In this paper we have provided an illustration that investment has a very important role to sustain economic growth of a region through to formation of capital, technology and skills of the workforce. From the results of this paper explains that foreign investment (PMA) has an influence on economic growth in east java. This shows that if an increase in foreign investment causes an increase in economic growth. So that if there is an increase in foreign investment will cause economic growth in East Java to increase.

Furthermore, domestic investment (PMDN) has an significant on economic growth in East Java Province. This condition was influenced by several factors including: 1) Risk Country, namely a small domestic market which caused a low rate of return if capital and lack of supporting facilities such as transportation, skilled labor, and technology; 2) The development of domestic investment in East Java is still hampered by the complicated process of obtaining permits due to bureaucracy that has not integrated coordination between the relevant departments; 3) The lack of information about sources of funds from the banking sector that can be utilized to support project financing; and 4) Low quality and productivity of human resources so that the technology transfer plan has not been implemented well, and there is increasingly fierce competition in attracting domestic investment by developed and developing countries.

In an effort to increase investment both domestic investment and foreign investment in East Java, is still necessary take a number of proactive steps including creating conducive investment climate such as simplifying the process of obtaining permits and coordinating interdepartmental coordination through cutting bureaucratic channels. It is also necessary to create economic stability through programs of reform, deregulation, and bureaucratization in all aspects of economic development. With these efforts it is expected to be more attractive to investors to invest their capital in East Java Province.

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