5th Joint International Conferences on Business, Economics and Social Sciences (ICBESS) 2018

IICOS – AICMaR - AICAR

ARYADUTA Hotel, Manado, August 8 – 9, 2018

Hosted by:

Sekolah Tinggi Ilmu Ekonomi Indonesia Jakarta

Fakultas Ekonomi & Bisnis Universitas Sam Ratulangi
Fakultas Ilmu Sosial & Ilmu Politik Universitas Sam Ratulangi

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Backward and Forward Linkages of Productivity Effect from Foreign Direct Investment

Suyanto
University of Surabaya
Surabaya, Indonesia
suyanto@staff.ubaya.ac.id

Yenny Sugianti
University of Surabaya
Surabaya, Indonesia

Abstract- Productivity related to foreign direct investment (FDI) has been examined for the last two decades, but the findings are mixed. This paper contributes to shed the light by analyzing the backward and forward linkages of FDI-related productivity. By estimating manufacturing firms of Indonesia, the results shows that there is a positive backward linkage from FDI in local firms on domestic firms in upstream 3-digit industries. There is also a positive forward linkage from FDI in local firms in downstream industries. The findings implicate the demonstration effect and skill-training effect of foreign firms to local firms in the industrial line. The findings are robust under fixed effect model, general method of moment model, and instrumental variable model.

Keywords- backward and forward linkages, productivity, foreign direct investment, manufacturing, upstream and downstream firms

Categorized in Entrepreneurship and Innovation