CHAPTER VI

CONCLUSION AND RECOMMENDATION

6.1. Conclusions

The aim of this research is to estimate the effect of trade openness, capital formation, and foreign direct investment on Indonesian economic growth by quarterly data from 1993 to 2014. This study used Vector Error Correction Model (VECM) to get a proper estimation result. Based on the regression, it concludes some results as follow:

1. ADF unit root test shows that all variables are stationer at first difference where it is significant at 5%. As the consequences, this paper employed the first difference variables.
2. Johansen Co-integration test indicates significant long run relationship between variables. This finding supported by the two co-integrating equations.
3. VECM stability imposes one unit root of modulus, however it is free from any problems that proved by classical assumptions tests and supported by the same findings from Becketti (2013) and Altaee, et al (2015).
4. The long run VECM shows that only foreign direct investment has strong and positive relationship with gross domestic product. Where the trace statistic (3.15367) is bigger than t table (2.36947 significant at 1%). This explains that the increasing of FDI will lead to the increasing of national’s GDP.

5. The short run VECM shows all variables have strong and positive relationship with Indonesian GDP.Trade openness significantly has relationship with GDP where t statistic is bigger than t table (1.86102 > 1.66235) at alpha 5%. Manwhile capital formation shows strong relationship in almost lag (lag 2, 3, 4, 5) where t statistics are 1.38907, 3.13551, 2.65847, and 2.91810 which mean bigger than t table (1.66235 and 2.36947). lastly, FDI also show positive and significant relationship with GDP where the t statistic is bigger than t table (1.84351 > 1.66235). These findings also supported by some previous literature review about trade openness and gross domestic product
6. Impulse response function of GDP to capital formation and FDI shows negatively in first period. This finding conctradicts with theory that CF and FDI has positive relationshp with GDP. This response is caused by the economic crisis in Indonesia that make some problems and cause economic growth decrease.
7. The robustness test is employed to see the validity of model. Figure 5.7, 5.8, 5.9, and 5.10 show the robustness test of each variable. The result is lag 4 and lag 6 have same movements with lag optimal which is lag 5. This proves that vector correction model is valid.

6.2 Recommendations

Based on the analysis and discussion, it can give some suggestions that may be useful for:

1. Government - as consideration for increasing Indonesian economic growth by improving trade openness, capital formation, and foreign direct investment.
2. Society – as reference and knowledge about economic growth, trade openness, capital formation, and FDI.

Future Researchers - as reference material for further research. It advised to try using another methods and variable or more variables used in this study, in order to get various result.This research also expected to give information for the political sector, investment sector, and other analysis policy to compare with this study.