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IMPACT OF FINANCIAL MARKET DEVELOPMENT ON GLOBAL COMPETITIVENESS AND FOREIGN DIRECT INVESTMENT

Batsyeba Sundari[1*], Pradivta Alfatihah[2]
Economic Department, Gunadarma University
**Coresponding Email*: batsyeba.sundari@gmail.com

ABSTRACT

This study aims to test and analyze the impact of financial market development (FMD) on the global competitiveness index (GCI) and Foreign Direct Investment (FDI), case study in Indonesia during the 2007-2017 period. This study was analyzed by using linear regression to test the relationship or influence of the dependent variables and independent variables. This study employs a quantitative approach with secondary data obtained from global competitiveness report and Investment Coordinating Board website. The study revealed that eight indicators used to measure FMD were affected positive significant. The study also shows that FMD affects positive but insignificant on GCI and same results for GCI on FDI.

Keywords: FDI, FMD, GCI

1. INTRODUCTION

Economic integration due to globalization which includes the openness of trade activities between countries or companies within the scope of the world has an impact on the increasingly competitive economic competition. The world economy is in line with the openness of the domestic economy to penetration from abroad, pointing to investment as an important thing in order to support the continuity of a country's development. The rise in globalization resulted in rapid changes and mobility of technologies and internationalization of production of goods and services through Foreign Direct Investment (FDI) (Gamariel and Hove, 2019).

Foreign Direct Investment (FDI) is the type of investment that has the strongest relationship to support economic growth and improve national competitiveness. According to Popovici and Călin (2015), FDI are seen as of source of competitiveness through their characteristic of being a capital flow that also provides technology and knowledge transfer from the home country to the host country. Positive influence of FDI on economic growth supports the idea to engage significant efforts to attract FDI (Zlatković, 2016).

Figure 1. FDI Realization in Indonesia By Investment Coordinating Board (BKPM)

Indonesia as a developing country has become a destination for foreign investors to invest their capital. Figure 1, shows the empirical development of FDI in Indonesia which tends to increase. The amount of foreign investment (FDI) during the period 2007 to 2017 has increased from year to year, although there was a decrease in 2009 due to the impact of the global crisis in 2008. The highest investment value occurred in 2017 with value of FDI realization of 32,239.80 million US$.

Factors that can be used in determining the increase in FDI refer to the pillars that are taken into account to calculate the Global Competitiveness Index, as provided by the World Economic Forum. The global competitiveness index is considered to be able to offer a broad scope of competitiveness and has good visibility among foreign investors. Competitiveness is vital for enhancing the economic growth that leads to rising of the living standards particularly in the small opened economies dependent on a great extent on FDI (Popovici and Cantemir Călin, 2015). According to Raeskyesa and Suryandaru (2020), there is a positive relationship between FDI inflow and competitiveness. The concept of competitiveness has been applied by Michael Porter widely, ranging from competitiveness in companies and industries to competitiveness on a national and global. Competitiveness as the set of institutions, policies, and the factors that determine the level of productivity of a country (Porter and Schwab, 2008). The capability to enhance the country's productivity will create the possibility not only to increase the country’s income level but also becomes the factor of its return on investment, which is one of the important factors to explain economic growth prospects (Ali, 2017).

Since 1979, the World Economic Forum has published a Global Competitiveness Report which includes the Global Competitiveness Index (GCI) to measure the competitiveness of various countries in the world. The global competitiveness index can be defined as an index to measure how efficiently a country utilizes its production factors in order to maximize total factor productivity (TFP) so as to achieve long- term economic growth (Nadya, Damia and Riza, 2020). Based on Global Competitiveness Report, Indonesia's global competitiveness index ranking dropped from 45 out of 140 countries in 2018 to 50 out of 141 countries in 2019.

The level of competitiveness of a country depends on its industrial capacity to innovate, be able to upgrade, and be consistent in terms of developing its industry both in terms of products, facilities, or the system applied. Financial development will boost productivity. In a report released by the World Economic Forum, Indonesia's financial market position in 2019 was ranked 58 out of 141 countries. Indonesia has a stable financial market with a score of 64,0 on a scale of 0-100 which is an improvement compared to 2018 considering the stage of development and development of the state's financial system.

Financial markets are an important component in the transmission of monetary policy and play an important role in promoting financial stability. Financial market development (FMD) aims to increase the capacity of the financial system to accumulate domestic savings and foreign capital to finance investment and consumption. The development of a country's financial market has a direct impact on its global competitiveness index and shows the productivity of an economy that contributes to the growth and prosperity of an economy (Yadav, Khandelwal and Singh, 2020). In this study, to analyze the competitiveness of financial market development is based on the parameters indicated by the World Economic Forum (WEF), which include Availability of financial services (AVS), Affordability of financial services (AFS), Financing from local equity market (FLEM), easiness of access to loans (EAL), Venture capital availability (VCA), Soundness of banks (SOB), Regulation of securities exchanges (RSE) dan Legal rights index (LRI).

Business investment is critical to productivity. Therefore economies require sophisticated financial markets that can make capital available for private-sector investment from such sources as loans from a sound banking sector, well-regulated securities exchanges, venture capital, and other financial products. In order to fulfill all those functions, financial markets need appropriate regulation to protect investors and other actors in the economy at large (Schwab, 2016). According to Alomari, Marashdeh and Bashayreh (2019), reveal that Financial market development (FMDG) were positive and significant, which indicates the existence of relationship from those variables to competitiveness in the context of growth.

Competitiveness is also one of the factors that can affect the foreign investment into a country. This is supported by research Popovici and Calin (2012) which found that there was a positive relationship between competitiveness indicators and FDI. The relationship between competitiveness and foreign direct investment is also carried out by Dunning and Zhang (2008) find that the level of competitiveness does, in general, encourage both inward and outward FDI. The global competitiveness index can be used as an indicator for measuring foreign direct investment because it is considered to be able to offer a broad scope of competitiveness and has good visibility among foreign investors.

2. METHODOLOGY

This study employed annual secondary data. Secondary Data refers to information collected from existing sources (Sekaran, 2017). Data were taken from the Global Competitiveness Report published by World Economic Forum, which is in the form of an annual report on Indonesia's competitiveness index.

Meanwhile, other supporting data are taken from the World Bank, the Investment Coordinating Board (BKPM), and Indonesian Central Statistics Agency during 2007 to 2017.

The study employs linear regression analysis to test the proposed research hypothesis over the period. This study uses Linear regression analysis is an analysis to determine the influence or linear relationship between the independent variable and the dependent variable. The analytical tool used in this research is SPSS version 22 software. SPSS is a computer program used to perform statistical data processing.

The object of this research is in Indonesia with the scope of analyzing to determine the effect of financial market development, global competitiveness index, and foreign direct investment. This study includes 3 (three) regression calculations to find results based on research objectives. First, to analyze the financial market development based on the parameters indicated by the World Economic Forum (WEF) which includes eight measurement indicators. Second, to analyze the impact of financial market development (FMD) on the global competitiveness index (GCI). And then third, to analyze the impact of the global competitiveness index (GCI) on foreign direct investment (FDI).

3. RESULT AND DISCUSSION

3.1 Result

The analysis technique used a quantitative approach. Tests were carried out using the SPSS program. There is a classical assumption test before calculating linear regression. Variables on this study were normally distributed and met the normality test's data requirements with a significance level > 0.05. The linear regression results are presented in the following tables.

Table 1. F Test

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.355	8	.044	27.254	.036[b]
	Residual	.003	2	.002		
	Total	.358	10			

a. Dependent Variable: FMD

b. Predictors: (Constant), X1, X2, X3, X4, X5, X6, X7, X8

Table 1 shows the results of the ANOVA output. ANOVA or analysis of variance, namely the regression coefficient test together (F test) to test the significance of the effect of several independent variables on the dependent variable. The independent variables including Availability of financial services (AVS) (X1), Affordability of financial services (AFS) (X2), Financing from local equity market (FLEM) (X3), easiness of access to loans (EAL) (X4), Venture capital availability (VCA) (X5), Soundness of banks (SOB) (X6), Regulation of securities exchanges (RSE) (X7), and Legal rights index (LRI) (X8), and the dependent variable was Financial Market Development (FMD) .The test uses a significance level of 0,05. The test results in this study obtained a calculated F value of 27.254 with a significance level of 0,036 < 0,05. This result means that the variable availability of financial services, affordability of financial services, financing through local equity market, ease of access to loans, venture capital availability, soundness of banks, regulation of securities exchanges, and legal rights index simultaneously affect on Financial Market Development.

Table 2. Linear Regression Test

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	4.060	.878		4.623	.001
	FMD	.098	.203	.158	.481	.642

a. Dependent Variable: GCI (Y)

Source: Data has been processed using SPSS 22.0 (2021)

The results of the analysis in table 2 show that the t-count value is 0.481 with a significance level of 0,642. The significance level is greater than 0,05. This means that variable financial market development partially has no significant effect on the Global Competitiveness Index.

Table 3. Linear Regression Test

	Unstandardized Coefficients		StandardizedCoefficients		
Model	B	Std. Error	Beta	t	Sig.
1 (Constant)	-140853.838	87490.026		-1.610	.142
GCI	36375.258	19515.054	.528	1.864	.095

a. Dependent Variable: FDI
Source: Data has been process using SPSS 22.0 (2021)

Table 3 shows that the t-count value is 1,864 with a significance level of 0,095. The significance level is greater than 0,05. This means that the Global Competitiveness Index (GCI) partially has no significant effect on the value of foreign direct investment (FDI).

3.2 Discussion

The first results state that the eight factors above have a positive and significant effect simultaneously on the financial market development variable. Financial market development is one of the pillars of global competitiveness. The result from Table 1 shows that the F-Test are significant at the 0,036 level. These value shows that all of the independent variables are able to explain the behaviour of the dependent variable. The results of the study are in accordance with the theory issued by the World Economic Forum, through the Global Competitiveness Report, that the indicators used to measure the aggregate value of the pillars of financial market development include availability and affordability of financial services, financing through equity markets, ease of access to loans, venture capital availability, restrictions on capital flows, bank soundness, regulation of securities exchanges, and the legal rights index.

Second results state that financial market development has a positive but not significant effect on the Global Competitiveness Index. The global Competitiveness score of World Economic Forum that is defined as the set of institutions, policies, and factors that determine the level of productivity of a country. The productivity of a country determines its ability to sustain a high level of income; it is also one of the central determinants of its return on investment, which is one of the key factors explaining an economy's growth potential. The financial market plays a strategic role in the national economy. The financial markets play a strategic role as source of economic financing, channel of transmission for monetary and fiscal policy as well as safeguard to preserve financial system stability. Future strategic financial market development initiatives in Indonesia must be oriented towards achieving qualities of deep and globally competitive financial markets. Such qualities are: (i) ability to provide alternative sources of financing and investment; (ii) ability to facilitate risk mitigation; and (iii) ability to promote transaction efficiency by refining the quality of financial market infrastructure (Bank Indonesia, 2018). Countries with better-developed financial systems tend to grow faster over long periods of time, and a large body of evidence suggests that this effect is causal: financial development is not simply an outcome of economic growth; it contributes to this growth (World Bank). The results of the study are in line with those of research conducted by (Rusu and Toderascu, 2016) and (Alomari, Marashdeh and Bashayreh, 2019).

Third results state that the global competitiveness index has a positive but not significant effect on Foreign Direct Investment. FDI inflows are often associated with additional beneficial effects, such as increased employment, enhanced management skills, new technologies, and higher wages (Vukšić, 2013). The high confidence of foreign investors in the investment climate in Indonesia has led to an increase in the flow of foreign funds (capital inflow) into the domestic financial market. This is indicated by the increasing realized value of foreign investment in Indonesia every year, as shown in figure 1. The results of the study are in line with research conducted by (Dunning and Zhang, 2008) and (Popovici and Calin, 2012) which states that there is a positive relationship between the competitiveness indicator and FDI.

4. CONCLUSION

The aims of this study was to determine the effect of Availability of financial services (AVS), Affordability of financial services (AFS), Financing from local equity market (FLEM), ease of access to loans (EAL), Venture capital availability (VCA), Soundness of banks (SOB), Regulation of securities exchanges (RSE) and Legal rights index (LRI), simultaneously on the value of pillars financial market development, the influence of financial market development on global competitiveness index, and the influence of the competitiveness index on the value of foreign direct investment in Indonesia. The results reveal that the eight indicator which is conduct by World Economic Forum have a positive significant effect simultaneously on the financial market development variable. Financial Market Development has a positive but not significant effect on the Global Competitiveness Index. And, The Global Competitiveness Index has a positive but not significant effect on Foreign Direct Investment, a case study in Indonesia, during the research period from 2007-2017.

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