FDI spillovers in Indonesia's chemical industry: a stochastic production frontier analysis

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Abstrak

There has been increasing role of Foreign Direct Investment (FDI) in developing countries since the 1980s. Interestingly, FDI is not only expected to bring direct effects, but also indirect effects or "spillovers" to a hosti economy. This paper aims to investigate FDI spillovers in the Indonesia's chemical industry, whether domestic firms benefit or not from foreign invesment. A stochastic production frontier approach is adopted to a firm level panel data for the periode of 1998-2000. There are three important findings. First, there is a clear hierarchy of technical efficiency of chemical firms based on their ownership status. Foreign owned firms have the highest level of technical efficiency, followed by joint ventures and domestic firms. Second, even though this paper confirms positive spillovers in the industry, the magnitude is relatively small. It shows that the Indonesian chemical industry has not yet been able to take full advantage of foreign presence. Third, a wider technology gap between domestic and foreign firms results in a higher spillovers. Findings of this paper imply that more FDI inflow into the Indonesia's chemical industry may benefit the industry. However, understanding the process of how the foreign presence affects domestic firms is important to take full advantage of the foreign presence.