

The Role of Foreign Investment and Domestic Investment in Indonesia's Gross Domestic Product (GDP)

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ABSTRACT

This research is important to provide a clear picture of Indonesia's economic dynamics and to support better decision-making in economic policy. Increased domestic investment is not enough to drive overall economic growth, and foreign investment is also not in line with the increase in domestic investment due to a mismatch between domestic investment and expected economic growth outcomes. The purpose of this study is to analyze the role of foreign investment and domestic investment on Indonesia's Gross Domestic Product (GDP). This study uses time series data from 2014-2023. The results of this study indicate that Foreign Direct Investment (FDI) does not have a significant positive effect on Indonesia's Gross Domestic Product (GDP). Although it shows a positive direction, the effect is not significant, so increasing foreign investment is still needed to drive the growth of Indonesia's Gross Domestic Product (GDP). Domestic Direct Investment (DDI) has a significant positive effect on Indonesia's Gross Domestic Product (GDP). This indicates that PMDN significantly contributes to GDP growth in Indonesia, with a stronger role than foreign investment. Simultaneously, foreign investment and domestic investment had a positive and significant impact on Indonesia's Gross Domestic Product (GDP) from 2014 to 2023. This indicates that although domestic investment had a partial negative impact, both simultaneously still made a positive contribution to economic growth.

INTRODUCTION

Indonesia, as the world's fourth-most populous country and endowed with abundant natural resources, has significant investment potential. Despite its rich natural resources, the challenge lies in suboptimal human resource management. However, current global economic dynamics present complex challenges. Indonesia's economic growth following the COVID-19 pandemic has shown a positive trend, but it continues to face pressure from global inflation, increases in the Fed's benchmark interest rate, and geopolitical uncertainty impacting international capital flows (IMF, 2023). In addition, the uncertainty of the global supply chain due to the Russia-Ukraine war increases energy and food costs, which in turn affects the attractiveness of investment in developing countries, including Indonesia (UNCTAD, 2022). This situation demonstrates that the Indonesian economy is not only influenced by domestic factors but is also highly vulnerable to external shocks. To achieve a just and prosperous society in accordance with Pancasila and the 1945 Constitution, sustainable and democratic economic development is necessary. Increasing investment, both domestic and international, is crucial for transforming economic potential into real economic strength (Polii et al., 2021).

Investment in a country can come from Domestic Direct Investment or Foreign Direct Investment, both of which have the potential to boost the economy. Investment can be direct, such as purchasing assets or establishing new businesses, or indirect, such as in the money and capital markets. FDI can serve as additional capital, but its impact tends to be short-term if it only meets needs that DDI cannot meet. However, FDI can also bring innovation and stimulate economic growth. Nevertheless, the Indonesian government prioritizes DDI to manage strategic sectors and improve provincial economies, thereby improving the national economy (Kambono & Marpaung, 2020); (Hapsari & Prakoso, 2016).

Theoretically, the relationship between investment FDI and DDI and economic growth can be explained through the Harrod Domar Growth Model which emphasizes the role of capital accumulation in increasing national output (Domar, 1946). In the context of developing countries,

Endogenous Growth Theory Romer, (1990) adds the dimension that investment not only increases the capital stock, but also brings technology, innovation, and increased productivity. Another relevant theory is the Eclectic Paradigm (OLI Framework) by (Dunning, 1988), which explains that foreign investment enters a country due to advantages in ownership, location, and internalization. This is relevant to understanding why FDI has a different impact than DDI on Indonesia's GDP.

According to Jamil & Hayati, (2020), Foreign direct investment (FDI) is a strategic source of foreign funding to support national development, particularly in the development of the real sector, which is expected to create jobs. The important role of FDI in Indonesia's economic development is also reflected in Law No. 25 of 2007 concerning Investment, which serves as the legal basis for investment activities in Indonesia. According to Sucipto & Puspitasari, (2016), To boost the economy, new investment is needed as an additional capital stock. Each additional capital stock will increase total output according to the capital-output ratio. Increased investment encourages growth in the private sector and households in resource allocation, which ultimately increases GDP. Thus, foreign investment has a positive relationship with GDP. Domestic Investment is an investment activity carried out by domestic investors in the territory of the Republic of Indonesia, using capital from within the country. DDI is part of the wealth of the Indonesian people, including rights and assets owned by the state and the private sector. Domestic Direct Investment (DDI) is the key to national economic growth, reflecting effective demand and creating productive efficiency for the future. Investment in capital goods not only increases production but also creates jobs, (Tamba et al., 2023)

According to Tamba et al., (2023), Investment in the national accounts or GDP structure is defined as the formation of domestic fixed capital. Investment is an important component of aggregate demand and crucial for sustainable economic development. Indicators of success include national income per capita and stable GDP growth. Economic development involves production across all sectors, requiring the construction of factories, buildings, and the provision of skilled labor and supporting facilities that require investment funds. According to Nuritasi, (2013) states that developing countries' economies require investment to improve economic performance, one of which is through Domestic Investment sourced domestically. DDI functions as capital formation, supports economic growth, increases production, and creates jobs, thus positively impacting the country's GDP.

According to Tamba et al., (2023) explains that Gross Domestic Product (GDP) is the total value of goods and services produced by production units within a country during one year. GDP reflects the market value of all final goods and services produced, and the higher a country's GDP, the better its economic performance, making it an indicator of economic growth. Economic activity in a country involves production by citizens, state-owned enterprises, and the private sector. Gross Domestic Product (GDP) is the total value of goods and services produced in a country, both by citizens and by foreign nationals working there. GDP reflects the country's economic capacity and growth, (Tamba et al., 2023).

International trade poses risks to Indonesia's economic stability, particularly due to a trade deficit that threatens domestic industry and creates dependence on imports. This can lead to industrial bankruptcy, job losses, and a decline in national income. Open trade policies also increase the risk of external shocks affecting public welfare, as occurred during the 2009 US economic crisis, which negatively impacted Indonesia's economic growth, (Riyad, 2012). Domestic Investment (FI) plays a crucial role in economic growth by increasing the supply of capital goods, such as new machinery and buildings. This contributes to increased economic output and, in turn, increases GDP, (Putri, 2017).

Table 1. Development of GDP and Investment in Indonesia 2014-2023

Year	GDP	DDI	FDI
2023	12301394	674923429	50267512
2022	11710248	552768972	45604963
2021	11120060	447063646	31093069
2020	10722999	413535524	28666272
2019	10949155	386498389	28208761
2018	10425852	328604916	29307908
2017	9912928	262350547	32239752
2016	9434613	216230848	28964075
2015	8982517	179465867	29275941
2014	8564866	156126157	28529699

Source: BPS Data, 2024

From 2014 to 2023, Indonesia's Gross Domestic Product (GDP) showed a general upward trend. Domestic Direct Investment experienced significant growth during this period. Meanwhile, Foreign Direct Investment also showed stable growth, although not as fast as DI growth. This reflects the investment dynamics in Indonesia, where DI is the main driver of economic growth, while FDI contributes more moderately.

Most previous studies emphasize the positive influence of PMA on Indonesia's economic growth (Kambono & Marpaung, 2020); (Hapsari & Prakoso, 2016). However, the results of this study show a different finding, namely a significant negative effect of DDI partially, although simultaneously it still contributes positively to GDP. This research gap lies in the lack of empirical studies comparing the simultaneous role of FDI and DDI in the post-COVID-19 pandemic period (2019-2023), when there was a drastic change in global investment flows (OECD, 2020). Thus, this study contributes to enriching the literature by providing the latest empirical evidence regarding the differences in the partial and simultaneous effects of FDI and DDI on Indonesia's GDP, and emphasizes the need for a balanced investment policy strategy between foreign and domestic capital.

METHOD

This study uses a quantitative research type with a descriptive analytical approach. This study aims to analyze the influence of Foreign Direct Investment (FDI) and Domestic Direct Investment (DDI) on Indonesia's Gross Domestic Product (GDP) in the period 2014-2023. The data used in this study are secondary data in the form of time series data that includes information related to GDP, DDI, and FDI from 2014 to 2023. The data was obtained from the Indonesian Central Bureau of Statistics (BPS). The population in this study is all annual data on GDP, DDI, and FDI recorded from 2014 to 2023. The sample used is available and relevant annual data, which includes data for each variable from a predetermined period. Data were collected through a documentation method using existing data sources, namely secondary data from the Central Bureau of Statistics (BPS) and official government reports related to GDP, DDI, and FDI. Data analysis in this study uses the multiple linear regression method. This analysis is used to determine the partial and simultaneous effects of the independent variables (PMA and PMDN) on the dependent variable (GDP). This study uses SPSS as a tool to perform linear regression calculations.

The hypotheses tested in this study are as follows:

Hypothesis 1: Foreign Direct Investment (FDI) has a partial positive and significant effect on Indonesia's GDP.

Hypothesis 2: Domestic Direct Investment (DDI) has a partial positive and significant effect on Indonesia's GDP.

Hypothesis 3: FI and DI simultaneously have a positive and significant effect on Indonesia's GDP.

To test the hypothesis, a multiple linear regression test was conducted using SPSS. This test was conducted to determine whether there was a significant effect of foreign investment (FI) and domestic direct investment on GDP, either partially or simultaneously. After conducting the regression test, a t-test (for partial effects) and an F-test (for simultaneous effects) were conducted to determine

whether each independent variable had a significant effect on the dependent variable (GDP). The significance level used was 0.05, (Kurniawan & Puspitaningtyas, 2016).

RESULTS & DISCUSSION

Multiple Regression Test Results

This research was analysed using multiple linear regression. This test was conducted using SPSS. This test aims to determine the influence of the independent and dependent variables. The results of the test are shown in Table 2 below:

Table 2. Multiple Regression Test Results

Model	Unstandarized Coefficients		Standar ized Coefficients	t	Sig	5% Confidence Interval for Bound		Correlations		
	B	Std. Error	Beta			Lower Bound	Upper Bound	Zero-order	Partial	Part
1 (Contant)	8484549	355592		23,86	,000	763707,73	9325391,097			
PMA	-,031	,016	-.204	-1,915	,097	-,068	,007	,723	-,586	-,119
PMDN	,008	,001	1,144	10,756	,000	,000	,010	,979	,971	,671

Source: processed data, 2025

It is known that the regression equation is as follows: $GDP = 8484549 + (-0.031) I_a + 0,008I_b + e$
PMA=FDI; PMDN=DDI

Based on Table 2, foreign investment has a significance value (sig) of 0.097, which is greater than 0.05, so the hypothesis is rejected and there is no significant positive effect on GDP, although it shows a positive direction. Increased foreign investment is needed to increase GDP. Meanwhile, domestic investment has a sig value of 0.000, less than 0.05, so the hypothesis is accepted and shows a significant positive effect on GDP growth in Indonesia. However, when viewed from the simultaneous influence, it is explained that foreign investment and domestic investment have a significance value (sig) of 0.000, which is less than 0.05, so the hypothesis is accepted, meaning that FDI and PMDN simultaneously have a significant positive effect on GDP (Table 3).

Table 3. Simultaneous Test Results (ANOVA)

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	1,20E+13	2	6,23E+12	125,091	,000
Residual	3,50E+11	7	4,98E+10		
Total	1,30E+13	9			

Source: processed data, 2025

The Effect of Domestic Investment on GDP

The research results show that Domestic Investment has a positive and significant impact on Indonesia's Gross Domestic Product (GDP). From 2014 to 2023, PMDN has increased annually, and GDP has also continued to rise. The post-monetary crisis situation has kept investment regulations stable, resulting in domestic investors' interest in continuing to invest. Each increase in PMDN contributes to an increase in GDP, meaning that domestic investment drives domestic economic activity such as increased production of goods and services, expansion of economic sectors, and job creation.

Therefore, increasing PMDN has a positive impact if labor is not available. This result contradicts research Jufrida et al., (2017) which found a positive and significant relationship. Domestic Investment continues to be increased comprehensively by improving workforce quality and optimizing resources to significantly impact GDP and economic growth. The government's role in creating a conducive investment climate is crucial in maintaining the growth of Domestic Investment (PMDN). Policies that support business ease, tax incentives, infrastructure development, and simplified licensing systems can further enhance investor confidence. Strengthening coordination

between central and regional governments, as well as ensuring legal certainty, will also attract more domestic investors. Consequently, a sustainable increase in PMDN will not only boost GDP but also promote inclusive and long-term economic development in Indonesia.

The Impact of Foreign Investment on GDP

The results of the study indicate that Foreign Direct Investment (FDI) has a positive but insignificant impact on Indonesia's Gross Domestic Product (GDP). Increased FDI is expected to boost GDP, but after the COVID-19 pandemic, FDI experienced an increase until 2023, while GDP continued to increase since 2014. In 2018, FDI decreased due to difficulties in the global economic situation that reduced foreign investor interest in investing in Indonesia.

The results of the study indicate that Foreign Direct Investment (FDI) has a positive but insignificant effect on Indonesia's Gross Domestic Product (GDP), in line with theoretical expectations but not statistical expectations. This study contradicts Kambono & Marpaung, (2020) which states that FI has a positive and significant influence, but is in line with (Tamba et al., 2023); (Jufrida et al., 2017), This explains the positive, though not significant, impact. Therefore, the government needs to implement a comprehensive strategy to promote FDI to make its impact on economic growth and GDP more significant.

This finding suggests that while FDI contributes to capital accumulation and technology transfer, its impact on GDP may be limited by factors such as low absorption capacity, bureaucratic barriers, and weak linkages between foreign and domestic industries. To enhance the effectiveness of FDI, Indonesia should focus on improving infrastructure, ensuring policy consistency, and increasing human resource competencies to support high-value investment sectors. Strengthening institutional quality and promoting sectors with high multiplier effects can also help maximize the long-term benefits of FDI for sustainable economic growth.

Simultaneous Influence of FI and DI on GDP

The results of the study indicate that at a significance level of 5 percent, with a statistical F probability or ANOVA of 0.000, $p\text{-value} < \alpha$ ($0.000 < 0.05$). This means that there is a significant simultaneous influence of foreign investment and domestic investment variables on GDP. The results of this study are consistent with previous research by Agustina et al., (2024) which explains that foreign investment and domestic investment have a positive and significant influence on economic growth.

This simultaneous influence indicates that both Foreign Direct Investment (FDI) and Domestic Investment (PMDN) play complementary roles in driving Indonesia's economic performance. FDI often brings advanced technology, management expertise, and access to international markets, while PMDN strengthens local industries and creates a stable production base. The synergy between these two types of investment contributes to overall economic expansion, enhances industrial productivity, and increases national competitiveness in the global market. Furthermore, the government must ensure that the benefits of investment are evenly distributed across sectors and regions to achieve inclusive growth. Encouraging collaboration between foreign and domestic investors, supported by consistent economic policies and a transparent regulatory framework, can maximize the impact on GDP. Additionally, efforts to improve infrastructure, digital transformation, and sustainable investment practices will reinforce the positive contribution of both FDI and PMDN to Indonesia's long-term economic development.

CONCLUSION

The results of the study indicate that Foreign Direct Investment (FDI) has a positive, but not statistically significant, effect on GDP. This indicates that while foreign investment can drive economic growth, its contribution was not strong enough during the study period, necessitating efforts to improve the quality and quantity of FDI to have a greater impact on GDP. Conversely, Domestic Direct Investment (DDI) was shown to have a positive and significant effect on GDP growth, indicating that DDI plays a stronger and more consistent role in supporting national economic growth. This finding underscores the importance of strengthening the domestic investment base as a primary driver of development. Furthermore, simultaneous analysis revealed that FDI and DDI together significantly contributed to GDP growth. Therefore, it can be concluded that although FDI is partially

insignificant, the combination of FDI and DDI still has a significant positive impact on the Indonesian economy.

However, this study has several limitations that should be considered. First, the data used only covers the period 2014-2023, so the results may not fully reflect long-term dynamics or more extreme global economic crises. Second, this study only used foreign direct investment (FDI) and domestic direct investment variables without considering other factors such as political stability, infrastructure, human resource quality, and external factors such as fluctuations in global commodity prices, which can also impact GDP. This limitation may affect the generalizability of the results; therefore, further research is recommended to expand the scope of the variables and the analysis period.

Practically, the findings of this study have important implications for national economic development. First, the government needs to strengthen incentive policies for domestic investors to ensure that domestic direct investment remains a key driver of growth, for example through fiscal support, ease of licensing, and increased access to financing. Second, strategies to attract FDI need to focus on productive sectors oriented toward exports, technology transfer, and job creation, rather than solely on the extractive sector. Third, the government also needs to ensure synergy between domestic and foreign direct investment by encouraging strategic partnerships, so that foreign investment can complement, rather than replace, domestic investment. Thus, a balanced investment policy is expected to increase national economic resilience while strengthening Indonesia's competitiveness in the face of global dynamics.

The findings of this study provide important insights into the relationship between Foreign Direct Investment (FDI) and Domestic Direct Investment (DDI) on Indonesia's Gross Domestic Product (GDP), while also offering valuable directions for future research and policy development. Future researchers are encouraged to elaborate further on their recommendations by focusing on improving workforce quality to better support the economic growth driven by domestic investment, conducting more in-depth analyses of specific sectors receiving investment to understand the differentiated impacts of FDI and DDI, and performing comparative studies with other countries that share similar economic characteristics to gain a broader perspective. Additionally, it is suggested to use broader and more diverse data, including those from the informal sector, to obtain a more comprehensive picture of the impact of investment on the economy.

The implications of this research indicate that both FDI and DDI play vital roles in influencing Indonesia's economic growth, particularly in the formulation of national economic policies. The results emphasize the importance of creating and maintaining policies that support DDI, given its positive and significant effect on GDP. At the same time, since both FDI and DDI contribute simultaneously to economic development, it is essential for the government to balance efforts in attracting foreign investors while also empowering domestic investors. Furthermore, improving infrastructure and developing human resources are crucial steps to ensure that investments contribute effectively and sustainably to the economy. The study also suggests that overreliance on FDI may expose the economy to risks in times of global instability; therefore, strengthening domestic investment can enhance national economic resilience. By increasing DDI, it is expected that more employment opportunities will be created, leading to higher national income and improved community welfare.

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