

Abstract

This research aims to analyze the relationship between agglomeration economies and international investment in the service industry, as an approach to test Dunning's Eclectic Paradigm (1979) along with Industrial Agglomeration theories by Weber (1909) and Marshall (1920). These theories suggest that multinational companies (MNCs) tend to invest in locations where firms of the similar industry are in close proximity to each other. Agglomeration economies are represented through Location Quotient (LQ) by Hoover (1936). Meanwhile, the proxy used for international investment is the annual Foreign Direct Investment (FDI) on the current currency. This study uses Fixed Effect and Ordinary Least Square (OLS) models to analyze the relationship between LQ and FDI. Data used in this research covers 32 provinces in Indonesia from 2013-2017. Through the OLS approach, this research concludes that there is a positive and significant relationship between LQ and FDI in Indonesia.

Keywords: Foreign Direct Investment, agglomeration economies, Location Quotient, service industry, Ordinary Least Squares