Analysis of Factors Affecting Private Investment in East Ogan Komering Ulu (East Oku)

Arjuna Sumarto

STIE Trisna Negara, East Oku, Sumatra Selatan, Indonesia

Abstract: This study aimed to analyze the effect of government spending, Economic Growth, Inflation, Interest Rate on Investment East Oku period 2014-2018. The data used are secondary time series data 2014-2018. The results showed that government spending, economic growth, inflation, and interest rates influence the amount of Domestic Investment (PMDN). Government spending and economic growth have a positive effect on Domestic Investment (PMDN). While inflation and interest rates, both of these variables have a negative influence on East OKU Domestic Investment.

1 INTRODUCTION

Exports and investments play an important role in an open country's economy. Exports will generate foreign exchange; foreign exchange will be used to finance imports of raw materials and capital goods needed in the production process, which will form added value to the economy. The aggregation of the added value generated by all production units in the economy is the Gross Domestic Product. Investment or investment is a component of forming national value-added, which is the purchase of capital goods and production equipment to increase the ability to produce goods and services available in the economy.

Increased economic activity is highly dependent on capital flows for productive ventures. Some experts say that exports and investment are "engines of growth". Therefore, high and sustainable economic growth rates are generally supported by increased exports and investment.

The economic theory defines investment as expenditures to buy capital goods and production equipment to replace and especially adding capital goods in the economy that will be used to produce goods and services in the future.

In other words, investment means shopping activities to increase the production capacity of an economy (Sasana, 2008). Investment is the first step in development activities, and investment is essentially the beginning of economic development activities.

The dynamics of investment affect the high and low economic growth. The urgency of capital formation in the region has received attention and emphasis, that private investment plays an important role in shaping patterns of development in the region. This investment will lead to regional capital formation (Zaris, 1987).

From various economic theories explain that investment is a function of the interest rate. An increase in the interest rate will result in reduced investment spending, and conversely, a decrease in the interest rate will result in increased investment spending. The interest rate is a factor that determines the size of the investment made by the public (private) (Sukirno, 1994).

Lower interest rates will increase investment demand. High-interest rates can be an obstacle to private and public sector growth. Therefore low-interest rates are an important condition for encouraging private investment.

Several previous studies on private investment have been carried out by Radianto (1995), which shows that the GRDP variable and the interest rate variable are not able to explain the phenomenon of private investment in Maluku, only the variety of work departures can explain the variation of private investment. Variables of investment in the previous year, economic growth, development spending, exchange rates, and reform policies in the investment sector affect FDI (Kodoatie, 1998). Neo-

Classical Investment Theory shows that real GDP growth rates have a positive influence on private investment (Wai and Wong, 1982; Greene and Villanueva, 1991; Fielding, 1997). This is also known as the "selerator effect" (Ouattara, 2005). Also, the value of capital desired by a company has a positive effect on the level of demand (Bayai & Nyangara, 2013).

National income is the number of goods and services that can be produced by a country's economy in one period, where the high level of national income reflects the number of goods and services produced by that economy to multiply. To achieve a high level of national income, it is necessary first to attain a high level of employment opportunities and increase national production capacity. In other words, achieving a high level of employment opportunities means that national production capacity is in full use.

One component of national products undertaken by companies is investment expenditure (investment expenditure) so that investment is a function of national income. Several other studies on private investment include the element of government expenditure as a determining factor for the size of private investment in a country (Sakr, 1993; Haque, Husain, and Montiel, 1991; Naqvi, 2002; Ahmad, Imtiaz, and Qayyum, Abdul, 2008). These studies show that there is a positive relationship between government spending and private investment.

2 LITERATURE REVIEW

2.1 Investment

Investment can be interpreted as expenditure or investment expenditures made by companies to buy capital goods or production equipment to increase the ability to produce goods and services available in the economy. This increase in the number of capital goods enables the economy to produce more goods and services in the future (Sukirno, 2006).

There are three types of investment spending. First, investment in fixed goods (business fixed investment), which covers the equipment and structures that the business world buys for use in production. Second, housing investment (residential investment) covers new housing where people buy it to be occupied, or the owners of capital buy it for rent. Third, inventory investment includes raw materials and supporting materials, semi-finished goods, and finished goods (Herlambang, 2001).

2.2 Government Expenditure

Government expenditure is all purchases or payments for goods and services for the national interest, such as the purchase of weapons and government office equipment, road and dam construction, salaries of civil servants, armed forces, and others (Samuelson & Nordhaus, 1997).

Government expenditure consists of three main items which can be classified as follows: (a) government expenditure for the purchase of goods and services; (b) government spending on employee salaries, changes in employee salaries that have a macroeconomic process whereby changes in employee salaries will affect the level of demand indirectly; and (c) government purchases for payment transfers. A transfer payment is not the purchase of goods/services by the government in the goods market, but this post records payments or government giving directly to its citizens, for example, payment of subsidies or direct cash assistance to various groups of people: pension payments, repayment of government loans to the public. Economically, transfer payments have the same effect as employee salary posts, although administratively, they are different (Boediono, 2001).

2.3 Inflation

Inflation is an economic phenomenon related to its very broad impact on macroeconomics. Inflation plays an important role in influencing the mobilization of funds through informal financial institutions. Inflation is defined as a continuous and persistent increase in the general prices of an economy (Susanti, 2000). Inflation is a condition where there is a sharp price increase that lasts continuously for a long period. Along with the price increase, the value of money fell sharply also in proportion to the increase in those prices.

2.4 Interest Rates

Interest rates can be seen as income earned from savings. A household will make more savings if the interest rate is high because more income from savers will be obtained. At low-interest rates, people don't like to make savings because they feel it's better to make consumption expenses or invest rather than save. Thus, if the interest rate is low, the community tends to increase their consumption expenditure or investment expenditure (Sukirno, 2006).

3 RESEARCH METHODS

Research is carried out with library materials in the form of scientific writings and scientific research reports that have a relationship with the topic under study. Data collection techniques used are direct recordings in the form of time-series data (time series) within a period of 10 years (2001- 2010).

Sources of data obtained from the publication of the Central Statistics Agency (BPS) of South Sulawesi Province. Also, other data supporting this research were obtained from reading sources such as journals, articles, and reading books related to this research.

In analyzing the magnitude of the effects of independent variables on the dependent variable, the econometric model is used by regressing existing variables using the method Ordinary Least Square (OLS).

The issue to be discussed is the extent of the influence of Government Expenditures, Economic Growth, Inflation, and Interest Rates on investment in the transportation sector in Indonesia by using multiple linear regression analysis. Its function is as follows (Soekartawi, 1990):

$$Y = f(X1, X2, X3, X4) \quad (1)$$

Then the function is expressed in terms of Y and X then,

$$Y = \llbracket \alpha X1 \rrbracket ^\wedge (\beta 1)\, e^\wedge (\beta 2 X2 + \beta 3 X3 + \beta 4 X4 + \mu) \dots \dots (2)$$

The above equation is converted into multiple linear forms to:

$$\text{Ln } Y = \ln \alpha + \beta 1 \ln X1 + \beta 2 X2 + \beta 3 X3 + \beta 4 X4 + \mu \quad (3)$$

Where:
Y = Investment (rupiah)
α = Intercept / constant
β1 β2 β3 = Regression Coefficient X1 = Government Spending (rupiah) X2 = Economic Growth (Percent) X3 = Inflation (Percent)
X4 = Interest Rate (Percent)
μ = term of error

4 RESULTS

According to WW. Rostow and RA. Musgrave in Guritno (1995), the development of government spending is in line with the stage of economic development of a country. This was also experienced by Indonesia, where both the nominal and real value of total government spending continued to increase throughout the year. Using the latest state expenditure classification, state spending was classified as central government spending and regional transfers. Furthermore, central government expenditure can be divided into K / L and Non-K / L spending, which as a whole includes employee expenditure, goods expenditure, capital expenditure, grant expenditure, social assistance, debt interest payments, subsidies, and other expenditures. Meanwhile, transfers to the regions are divided into balancing funds as well as special autonomy funds and adjustment funds.

The development of prices of goods and services can still be relatively controlled, as seen from a fairly stable inflation rate, which is inseparable from government policies in a prudent monetary sector and tighter fiscal policies and is supported by the supply of consumer goods at sufficient quantities and reasonable price levels. A sharp decline in inflation occurred in 2003, which was at the point of 5.06%, which fell almost 50% from the previous year, namely in 2002 at the level of 10.03%. However, in 2005 inflation increased again, namely, at the point of 17.11% caused by the increase in fuel prices. Although, in the following years, the inflation rate can be suppressed, in 2008, inflation returned to an increase that reached the point of 11.06% because, in 2008, there was a crisis in the international world that caused domestic turmoil. In 2009 inflation had decreased, which was at 2.78% from the previous year, which reached 11.06%.

Classical Theory states that the decision of whether an investment will be made or not depends on the interest rate, which is the cost of the use of funds (Nopirin, 1992). The desire to invest will be smaller if the interest rate is high. This is because the amount of expenditure incurred by investors in investment will increase as a result of the high-interest rate, which is the cost of using funds (cost of capital) that must be paid for the investment fund. Conversely, the lower interest rates will increasingly encourage investors to invest. This is because the cost of using funds is getting smaller, so the expected level of profits is greater (Samuelson & Nordhaus, 1997).

5 DISCUSSIONS

5.1 Effect of Government Expenditure on Investment

The theory of state spending, outlines three stages that must be passed by each country. In the initial stages of economic development, large government is required for government investment, primarily to provide infrastructures such as roads, health, and education. In the intermediate stage of economic development, investment is still needed for economic growth, but it is hoped that private sector investment has begun to develop. Then in the advanced stages of economic development, government spending is still needed, primarily to improve the welfare of the community, for example, improving education, health, and social security. Another idea was put forward by Adolph Wagner. His empirical observations of European countries, the United States, and Japan in the 19th century show that in a country's economy, government spending will increase in line with the increase in the country's national income. So it can be said that government spending has a positive effect on investment.

5.2 Influence of Inflation on Investment

The Relationship between inflation and investment is negative. High inflation in a country, resulting in the minor money supply increased, then followed by high-interest rates, with interest rates that tend to be high, the investment will fall. High inflation also causes the purchasing power of the people to decline which then leads to reduced returns or investment returns, thereby reducing investor interest in investing. An investor will tend to invest if the inflation rate in a country is stable. This is because, with the stability in the inflation rate, the price level of goods, in general, will not increase significantly. Therefore, investors will feel more secure to invest when the inflation rate in a country tends to be stable or low. In other words, an increase in inflation will reduce the interest of investors to carry out investment, and otherwise, if inflation falls, the investment will increase.

5.3 Effect of Interest Rates on Investment

Interest rates used in this thesis research are real interest rates. Real interest rates are interest rates after being reduced by inflation (real interest rate = Nominal interest rate - inflation expectations). The relationship between interest rates and investment is negative.

The interest rate is one of the important factors that influence investment. Fluctuations in interest rates are a consideration for investors. If the interest rate is lower than what he expected, then someone will choose to invest their money rather than keep the money in the bank or lend the money to someone else. If investment funds are obtained from borrowing banks or other parties with an interest rates lower than the profits to be obtained, it can be used to cover the loan interest rate.

The higher the interest rate, the less the desire to invest. The reason is that an investor will increase his investment expenses if the expected return on investment is greater than the interest rate he has to pay for the investment fund, which is the cost of using the fund or the cost of capital. The lower the interest rate, the more motivated entrepreneurs, will be to invest because the cost of using funds is also getting smaller.

6 CONCLUSIONS

Government expenditure variables, economic growth, inflation, and credit interest rates simultaneously affect the domestic investment (PMDN) of the transportation sector in Indonesia. The government must oversee the economy through policies that are made so that the policy can further turn on the economy in Indonesia and be able to attract investors to invest more in Indonesia.

Government spending hurts domestic investment in the transportation sector in Indonesia. It means that every time there is an increase in the gross domestic product of the transportation sector, the domestic investment will increase. The government should divide spending according to type so that it can be known in more detail the effect of each type of expenditure on investment.

Inflation hurts domestic investment in the transportation sector in Indonesia. It means that every time there is an increase in inflation, the domestic investment will decrease. Maintaining the level of domestic inflation to remain stable, thereby

making domestic prices also remain stable so as to encourage increased domestic investment.

Interest rates have a negative effect on domestic investment in the transportation sector in Indonesia. It means that every time there is an increase in the interest rate, the domestic investment will decrease.

REFERENCES

Ahmad, I., & Qayyum, A. (2008). Effect of Government Spending and Macro-Economic Uncertainty on Private Investment in Services Sector: Evidence from Pakistan. European Journal of Economics, Finance and Administrative Sciences(11), 84-96. Retrieved from https://mpra.ub.uni-muenchen.de/11673/1/MPRA_paper_11673. pdf

Bayai, I., & Nyangara, D. (2013). An Analysis of Determinants of Private Investment in Zimbabwe For The Period 2009–2011. International Journal of Economics and Management Sciences, 2(6), 11-42. Retrieved from https://www.omicsonline.org/open-access/an-analysis-of-determinants-of- private-investment-in-zimbabwe-for-the- period--2162-6359-2-138.pdf

Boediono. (2001). Ekonomi Makro (4th ed.).Yogyakarta: BPFE.

Fielding, D. (1997). Adjustment Trade Policy and Investment Slumps: Evidence form Africa. Journal of Development Economics, 52(1), 121-137. doi:10.1016/S0304-3878(96)00437-3

Greene, J., & Villanueva, D. (1991). Provate Investment in Developing Countries: an Empirical Analysis. . IMF Staff Papers, 38.

Guritno, B. (1995). Analisis Pertumbuhan Tanaman. Yogyakarta: Gadjah Mada University Press. Haque, N., Husain, A., & Montiel, P. (1991). An

Empirical "Dependent Economy" Model for Pakistan. IMF Working Papers.

Herlambang, T. (2001). Ekonomi Makro. Jakarta: PT Gramedia Pustaka.

Kodoatie, J. M. (1998). An Analysis of Foregin Direct Investment in Indonesia (1971-1994). Media Ekonomi dan Bisnis, X(1-2).

Naqvi, N. H. (2002). Crowding-in or Crowding out? Modelling the Relationship between Public and Private Fixed Capital Formation Using Co-integration Analysis: The Case of Pakistan 1964–2000. The Pakistan Development Review, 41(3), 255-276. Retrieved from http://www.pide.org.pk/pdf/PDR/2002/Volu me3/255-276.pdf

Nopirin. (1992). Ekonomi Moneter (1st ed., Vol. 1). Yogyakarta: BPFE.

Ouattara, B. (2005). Modelling the Long Run Determinants of Private Investment in Senegal. University of Nottingham: Center for Research in Economic Development and International Trade. Retrieved from

https://www.nottingham.ac.uk/credit/docume nts/papers/04-05.pdf

Radianto, E. (1995). Spesifikasi Dinamis, Model Investasi Jangka Panjang: Sebuah Studi Kasus di Daerah Maluku. Jurnal Ekonomi dan Bisnis Indonesia, 10(1), 81-89.

Sakr, K. (1993). Determinants of Private Investment in Pakistan. IMF Working Paper, 93(30).

Samuelson, P., & Nordhaus, W. D. (1997).

Mikroekonomi. Jakarta: Erlangga.

Sasana, H. (2008). Analisis Faktor-Faktor yang Mempengaruhi Investasi Swasta di Jawa Tengah. Jurnal Ekonomi dan Kebijakan, 1(1), 1-10. doi:10.15294/jejak.v1i1.1445

Soekartawi. (1990). Teori Ekonomi Produksi: Dengan Pokok Bahasan Analisis Cobb Douglas. Jakarta: Rajawali Pers.

Sukirno, S. (1994). Pengantar Ekonomi Makro.

Jakarta: PT. Raja Grasindo Persada.

Sukirno, S. (2006). Ekonomi Pembangunan. Jakarta: Kencana.

Susanti, H. (2000). Indikator-indikator Makro Ekonomi. Jakarta: LPFE-UI.

Wai, T. U., & Wong, C. H. (1982). Determinants of Private Investment in Developing Countries. Journal of Development Studies, 19(1), 19- 36. doi:10.1080/00220388208421848

Zaris, R. (1987). Prespektif Daerah dalam Pembangunan Nasional. Jakarta: LPFE UI.