

Determinants of Indonesia Domestic Investment and Foreign Investment

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ABSTRACT

This research aimed to know how the effect of capital expenditure and inflation variable the Domestic and Foreign Investment in Indonesia especially Provinces on Java Island from 2016 to 2020. This research used the panel data regression method with time-series data from the Central Bureau of Statistics (BPS) and the Directorate General of Fiscal Balance's portal data. The results of this study are the inflation variable partially significant effect on Foreign Investment in provinces on Java Island. On the contrary, the capital expenditure variable does not have a significant effect both on domestic and foreign investment, while the inflation variable strengthens the relationship between capital expenditures and domestic investment.

Keywords: *Capital Expenditure, Domestic Investment, Foreign Investment, Inflation*

Introduction

Foreign and domestic investment is the first step in development activities and economic growth. However, in reality, Indonesia is still experiencing difficulties in terms of providing sufficient capital to carry out economic development. Indonesia cannot rely solely on foreign loans to obtain sufficient capital. This situation encourages developing countries such as Indonesia to look for other alternatives besides foreign loan assistance by promoting investment, especially Foreign Investment (PMA). According to Munir Faudy (2008), what is meant by direct investment is an investment model in which foreign or domestic parties buy directly (without going through the capital market) shares of national companies or establish new companies, either through the Investment Coordinating Board (BKPM) or through another

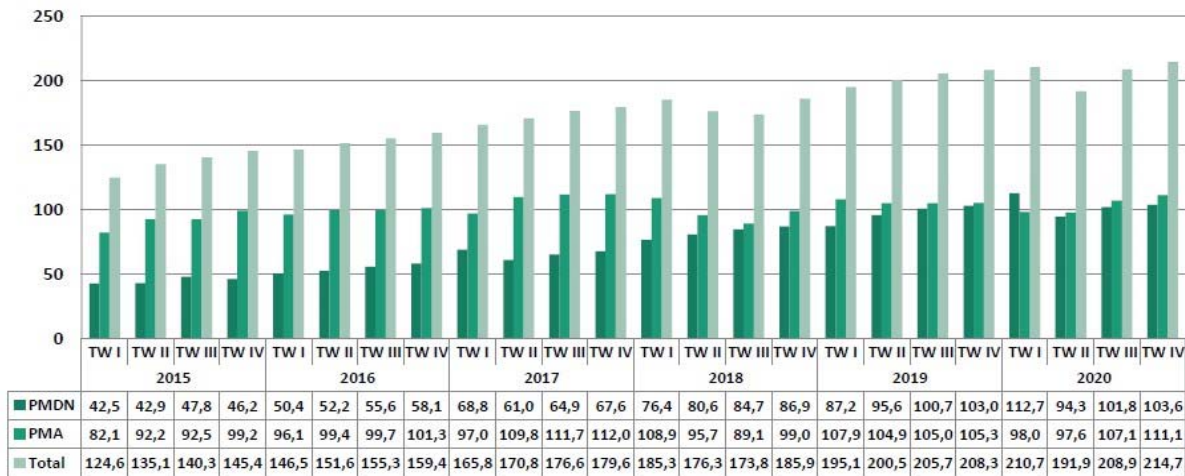


Figure 1. Progress of Investment Realization 2015 – 2020: per Quarter

The picture above shows how the development of PMDN and PMA in Indonesia. It can be seen that the rate of PMDN and PMA, in general, has the same upward and downward trend. Sufficient capital will lead to economic growth and will improve people's welfare, especially for entrepreneurs who need financial support to develop their businesses (Munir Faudy 2018). Through investment, foreign and domestic capital can make a better contribution to the process of development and economic growth. Investors will conduct a feasibility study, including forecast, prediction, and projection before investing their capital in one place. In investing, investors certainly want to get the maximum profit with the minimum amount of expenditure. The ability of investors to understand and predict future macroeconomic conditions is very useful in making profitable investment decisions. Macroeconomics describes economic changes that affect many parties such as society, companies, governments, and the foreign sector.

Inflation is an increase in commodity prices caused by out of sync between commodity procurement programs (production, pricing, printing money, etc.) with the level of income owned by the community. The high inflation rate causes goods and services to become less competitive which causes the profits obtained by the company to decrease, which in turn will inhibit new investment. Therefore, the higher the inflation rate, the lower the amount of foreign direct investment entering Indonesia.

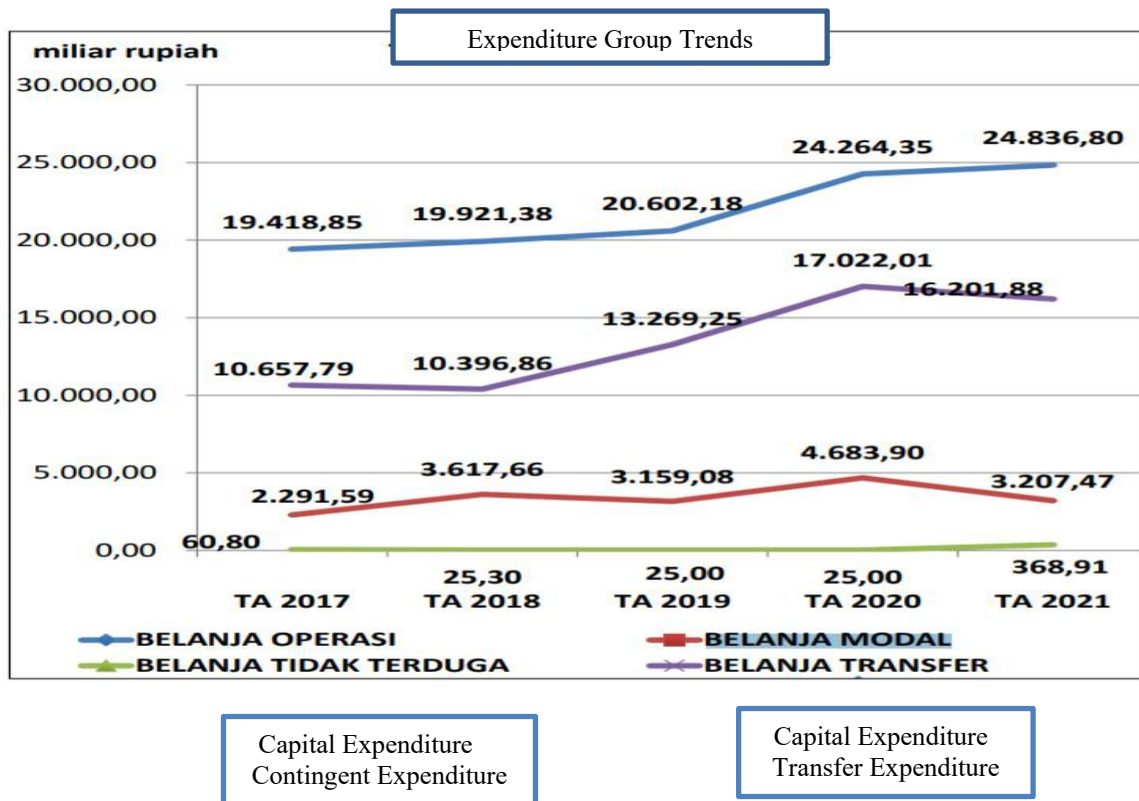


Figure 2. Expenditure Group Trends

Source: Regional Budget, Directorate General of Regional Financial Development, Ministry of Home Affairs 2017-2021

Regional expenditure, which is government expenditure, is an important component to overcome this. Regional expenditures are used by regional governments to manage the regional economy. Regional expenditures that will have an impact on economic growth both directly and indirectly include expenditures used for education, infrastructure, housing, health, subsidies, technology, and transfers. The novelty of this study is the variable Capital Expenditure and Inflation as moderating variable

The aims of this study are (1) to determine the effect of Capital Expenditure on PMDN and PMA, (2) to determine the effect of Inflation on PMDN and PMA, and (3) to determine whether Inflation strengthens the relationship between Capital Expenditure on PMDN and Capital Expenditure on PMA.

The core issues that will be discussed in this study are (1) whether capital expenditures have a significant effect on PMDN and PMA, (2) whether inflation has a significant effect on PMDN and PMA, and (3) whether inflation strengthens the relationship between capital expenditures on PMDN and capital expenditures against PMA.

Literature review

Capital expenditure

Capital expenditures are expenditures incurred to obtain fixed assets and assets that provide benefits for more than one period (Halim, 2014). Capital expenditures are identified as land expenditures, equipment and machinery expenditures, road, network and irrigation expenditures, building and building expenditures, and other theta asset expenditures.

Domestic investment

Domestic investment is one of the main keys to boosting economic growth. and reflects effective demand. It can create productive efficiency for products in the future. This process of investment generates national output in a variety of ways. Investment in capital goods not only increases productivity but also increases the use of labor. This investment will also have a positive impact, one example is that this investment will lead to specialization and broad production savings Munir Fuady (2018).

Foreign investment

The word investment has a broader meaning because it can include foreign direct investment (direct investment) and indirect investment (portfolio investment), while the word investment has more connotations of direct investment. Foreign investment has a different meaning among economists. According to Munir Fuady (2018) what is meant by direct foreign investment seen in a narrow sense is a model of foreign investment carried out in which a foreign party or foreign company buys directly (without going through the capital market) shares of a national company or establishes a new company, either through the National Board of Directors. Investment Coordination (BKPM) or through other departments. Direct foreign investment activities mean foreign investors are directly or physically present in their business. The presence or establishment of a business entity with the status of foreign investment, then the business entity must comply with the provisions and rules of law in force in Indonesia.

Inflation

Inflation is a condition in which prices in general experience a continuous increase while on the other hand, the income level of the community is relatively constant and if that happens, the process of impoverishment is taking place. The instability of a country's economy can be a barrier to entry of investment into a country. High inflation illustrates that the country's economy is unstable, which means that the country's government fails to balance the economy. Inflation can cause the level of risk of business failure to be even greater. The high rate of inflation reduces public consumption due to the declining ability of the public to buy goods due to soaring prices. Inflation prolonged, many producers will go bankrupt because their products will be relatively more expensive so that no one can afford to buy them. It can be concluded that there is a negative relationship between inflation and investment. That is, the more unstable a country's macro economy, the lower the level of investment.

From some of the factors mentioned above, the hypotheses to be formulated in this study are as follows:

H1: Capital Expenditure has a significant effect on PMDN H2: Capital Expenditure has a significant effect on FDI H3: Inflation has a significant effect on PMDN

H4: Inflation has a significant effect on FDI

H5: Inflation strengthens the relationship between Capital Expenditures and Domestic Direct Investment

H6: Inflation strengthens the relationship between Capital Expenditures and FDI

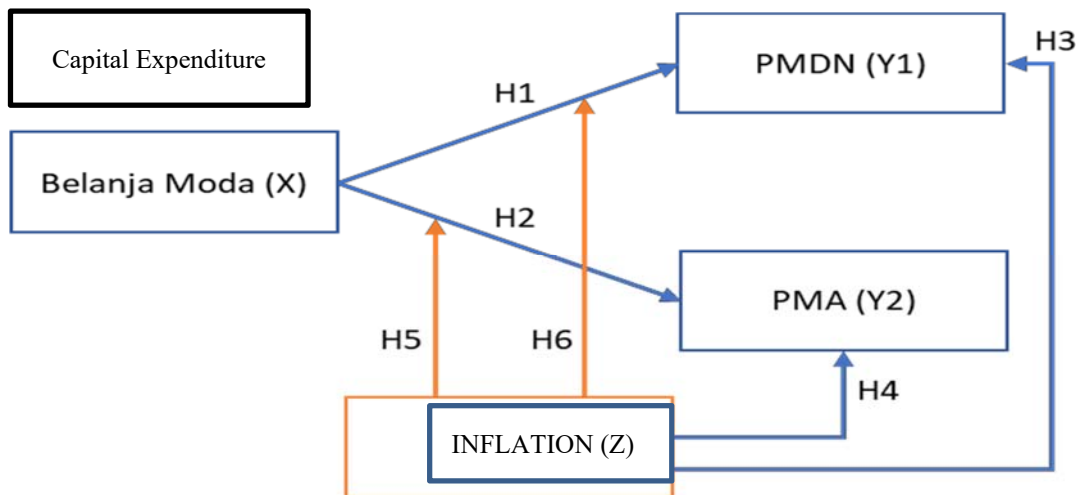


Figure 3. Conceptual framework

Research methods

Types of research

This research uses explanatory research with a quantitative approach.

The data for research activities are taken from the website of the Central Statistics Agency (BPS) and the data portal of the Directorate General of Fiscal Balance.

Measurement variable

a. Capital Expenditure

Based on PP No. 71 of 2010 concerning Government Accounting Standards, Sholikhah & Wahyudin (2014), the measurement of capital expenditure variables is measured by a ratio scale. Capital expenditures can be measured by calculating:

Capital Expenditure = Land Expenditure + Equipment and Machinery Expenditure + Building and Building Expenditure + Road, Irrigation, and Network Expenditure + Other Fixed Assets Expenditure + Other Asset Expenditure.

Capital expenditure data is taken from the data portal of the Directorate General of Fiscal Balance.

b. Domestic Investment (PMDN)

Data on foreign investment in this study is the value of foreign capital entering Indonesia by economic sector. The data used is data every year taken from BPS in billions of IDR.

c. Foreign Investment (PMA)

Data on foreign investment in this study is the value of foreign capital entering Indonesia by economic sector. The data used is data every year taken from BPS in units of Million USD.

d. Inflation

Inflation data used in this study is the percentage value of the inflation rate based on the Consumer Price Index (CPI) issued by Bank Indonesia every quarter for 9 years, starting from the first quarter of 2006 to the fourth quarter of 2014 in percentage terms (%).

Population and research sample

a. Population

The population used in this study is the overall data published by the Central Statistics Agency and the data portal of the Directorate General of Fiscal Balance regarding the variables studied.

b. Sample

Sampling in this study uses a purposive sampling technique. Purposive sampling is a sampling technique with certain considerations, Sugiyono (2011).

Data collection technique

The data used in this study is secondary data in the form of time series. Because the data used is secondary data, the data collection technique used in this study is the documentary method.

Conclusions and suggestions

Based on the results of the research and discussion that have been described in the previous section, the following conclusions can be drawn: (1) Capital expenditures have no effect on PMDN and PMA in the Provinces of Java for the period 2016 – 2020, (2) Inflation has no effect on PMDN, on the other hand, has a significant effect on PMA. This means that if there is an increase in inflation, it will reduce FDI in Provinces in Java Island for the period 2016-2020, and (3) inflation strengthens the relationship between capital expenditures and PMDN, but does not moderate capital expenditures and in Provinces in Java for the period 2016-2020.

Based on the results of the research and the conclusions that have been formulated, several suggestions from this research are put forward as follows: (1) Increasing government efforts in maintaining inflation stability in Java (2) Reviewing and reducing regulations that are burdensome for investors to invest in Indonesia, both domestic investment and foreign investment.

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Appendices A.**Secondary Data on Capital Expenditure, PMDN, PMA, and Inflation**

PROV	TAHUN	BM (X1)	PMDN (Y1)	PMA (Y2)	INFLASI (Z1)
JKT	2016	8,965.47	12,216.90	3,398.20	2.37
JKT	2017	11,045.72	47,262.30	4,595.00	3.72
JKT	2018	14,118.61	49,097.40	4,857.70	3.27
JKT	2019	11,551.93	62,094.80	4,123.00	3.23
JKT	2020	3,173.22	42,954.70	3,613.30	1.59
JBR	2016	2,859.36	30,360.20	5,470.90	2.75
JBR	2017	1,693.28	38,390.60	5,142.90	3.63
JBR	2018	3,145.85	42,278.20	5,573.50	3.54
JBR	2019	2,530.35	49,284.20	5,881.00	3.21
JBR	2020	1,672.91	51,400.50	4,793.70	2.18
JTG	2016	2,815.68	24,070.40	1,030.80	2.36
JTG	2017	1,454.60	19,866.00	2,372.50	3.71
JTG	2018	1,681.75	27,474.90	2,372.70	2.82
JTG	2019	2,530.35	18,654.70	2,723.20	2.81
JTG	2020	1,672.91	30,606.10	1,363.60	1.56
YOG	2016	836.87	948.60	19.60	2.29
YOG	2017	1,046.73	294.60	36.50	4.20
YOG	2018	1,132.83	6,131.70	81.30	2.66
YOG	2019	1,035.20	6,298.80	14.60	2.77
YOG	2020	940.63	2,683.40	9.70	1.40
JTM	2016	2,150.59	46,331.60	1,941.00	2.74
JTM	2017	3,090.06	45,044.50	1,566.70	4.04
JTM	2018	2,840.55	33,333.10	1,333.40	2.86
JTM	2019	2,770.97	45,452.70	866.30	2.12
JTM	2020	1,904.56	55,660.60	1,575.50	1.44
BTN	2016	1,334.13	12,426.30	2,912.10	3.96
BTN	2017	1,349.69	15,141.90	3,047.50	3.94
BTN	2018	1,362.55	18,637.60	2,827.30	3.44
BTN	2019	1,379.32	20,708.40	1,868.20	3.50
BTN	2020	994.26	31,145.70	2,143.60	2.22

Description:

JKT = DKI Jakarta Province

JBR = West Java province

JTG = province of Central Java YOG = DI Yogyakarta Province JTM = East Java Province

BTN = Banten Province

PMDN = Domestic Investment (in Billions of Rupiah) PMA = Foreign Investment (in Millions USD)

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Conflict of Interests

No, there are no conflicting interests.

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