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The Effect of Government Spending on the Inclusive Economic Development Index on the Island of Sumatra

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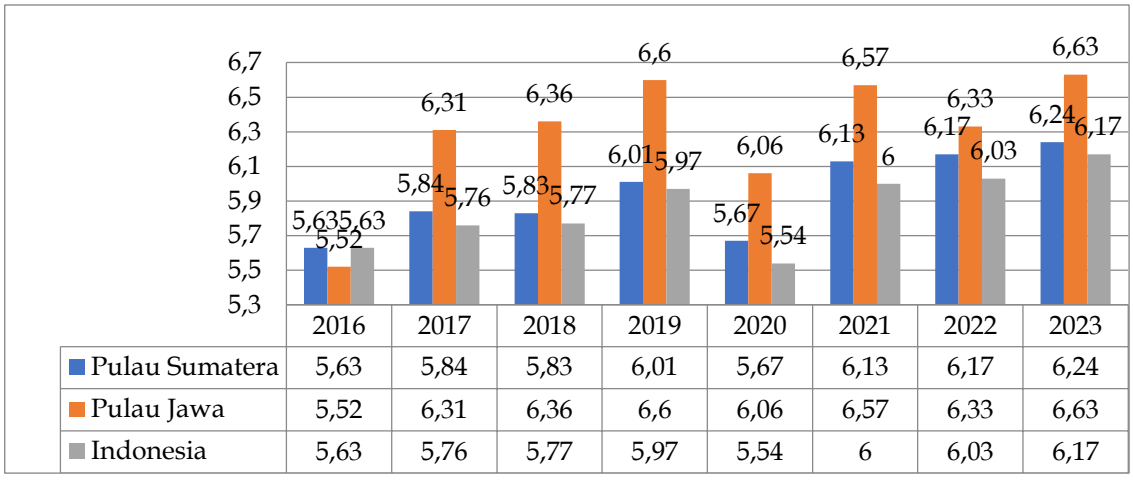
A B S T R A C T

This research is motivated by the high economic growth on the island of Sumatra. Sumatra Island has the second largest Gross Domestic Product (GDP) contribution in Indonesia, namely 21.4 percent and the third highest IPEI. This research aims to examine the influence of government spending on economic functions, public services, health and education on the Inclusive Economic Development Index (IPEI). This research uses the Panel Data Regression Method in 10 Provinces on the Island of Sumatra 2016-2023. The research results show that government spending on economic functions and public services has no effect. Meanwhile, Health and Education have a positive and significant influence on IPEI.

INTRODUCTION

Local governments are authorized by the central government to manage and make economic plans in accordance with the needs and conditions of their citizens. With fiscal decentralization, local governments have the authority to set budgets for economic development programs that have been planned to achieve predetermined goals. This ensures that economic development in the area runs effectively and produces welfare for the community. Inclusive economic growth is one way to measure the success of a region's economic development. Inclusive economic growth focuses on improving people's welfare rather than just increasing output. These welfare measures are based on reducing unemployment, inequality, and poverty, as well as equitable access to the economy, public services, health, and education.

The implementation of inclusive growth is also carried out by districts/cities on the island of Sumatra. During the eight-year period (2016-2023), the average IPEI on Sumatra Island was always above the IPEI of Indonesia and below that of Java. In 2018, the average IPEI on the island of Sumatra decreased to 5.83% from the previous 5.84%. This is inversely proportional to the average condition of IPEI in Java and Indonesia, which has actually increased. On the island of Java it became 6.36% from the previous 6.31% while in Indonesia it increased to 5.77% from the previous 5.76%. In 2019, the average condition of the IPEI of the two islands and Indonesia together increased with a figure of 6.01% for Sumatra Island, 6.60% for Java Island and 5.97% for Indonesia. This condition is inversely proportional when entering 2020 which resulted in the two islands and Indonesia together experiencing a decrease in IPEI with a figure of 5.67% for Sumatra Island, 6.06% for Java Island and 5.54% for Indonesia. Economic conditions began to improve when entering 2021, which directly resulted in an increase in the average IPEI. The average rate of IPEI on the island of Sumatra is at 6.13%, Java is at 6.57% and Indonesia is at 6.00%.



	2016	2017	2018	2019	2020	2021	2022	2023
Pulau Sumatera	5,63	5,84	5,83	6,01	5,67	6,13	6,17	6,24
Pulau Jawa	5,52	6,31	6,36	6,6	6,06	6,57	6,33	6,63
Indonesia	5,63	5,76	5,77	5,97	5,54	6	6,03	6,17

Source: BAPPENAS (2016-2023), processed

Figure 1 Graph of the Inclusive Economic Development Index of Sumatra, Java, and Indonesia

The island of Sumatra has the second largest contribution to Gross Domestic Product (GDP) in Indonesia, at 21.4 percent after Java Island at 59.3 percent and the third highest in IPEI. It's just that three of the 10 poorest provinces in Indonesia are on the island of Sumatra, namely Aceh at 14.75%, Bengkulu at 14.34% and South Sumatra at 11.78%. This percentage is a fairly high number, and only beats provinces in the Eastern Indonesia Region (BPS, 2023). This is an interesting phenomenon because the economic growth indicators of the island of Sumatra are among the highest and contribute greatly to the progress of the national economy, but this is not in line with the equal distribution of income with the entry of three of the ten poorest provinces in Indonesia.

Economic growth on the island of Sumatra may not have reached an optimal level and is less beneficial for the poor. There is also inequality between provinces on the island of Sumatra, as well as income inequality as seen from the Gini ratio, which is not satisfactory. This phenomenon shows that inclusive economic growth on the island of Sumatra has not fully occurred, especially in provinces and districts/cities. Therefore, to determine the level of economic inclusivity, it is necessary to measure using the inclusive economic development index set by the Ministry of National Development Planning/National Development Planning Agency.

The Inclusive Economic Development Index (IPEI) is one of the tools used to monitor and measure the level of development inclusivity at the district/city, provincial, and national levels in Indonesia. IPEI is formed through 3 pillars, 8 sub-pillars, and 21 indicators (Bappenas, 2018). Inclusive growth can be achieved with the role of the government. The role of the government is associated with physical policy, namely by allocating the budget effectively. In general, the budget issued by the government in each function fluctuates every year according to the needs of each region. Government spending is government spending that is pro-people, including spending on economic functions, public services, health and education.

The results of previous studies show several results. One of the results of the study said that health spending has a significant positive relationship with GDP in the United States Raghupathi & Raghu pathi (2020). Arrfah & Trisakti (2022) also concluded that the health function spending variable has a positive and significant effect on inclusive economic growth. In contrast to Faizin & Prabowo (2023) who stated that expenditure on health functions has no effect on PEI Growth Aspects and expenditure on education functions has a negative effect on Inclusive Economic Growth Growth Aspects Growth. In addition, a similar study was also conducted in East Java Province by Safitri (2021) for the period of 2014-2018. The results of the study explain that government expenditure on health and education functions has a positive and significant impact on the inclusive economic development index, both in the short and long term. However, the economic situation at that time was different from the period studied in this study, because at that time there was no COVID-19 pandemic that changed the economy in Indonesia.

Based on the above background, the author examines the influence of local government expenditure in the form of expenditure on economic functions, public services, health, and education on the inclusive economic development index on the island of Sumatra and uses case studies from 10 (ten) provinces between 2016 and 2023. This study adopts similar previous research research. However, this study has the most recent, namely in the variables used.

LITERATURE REVIEW

In N. Gregory Mankiw (2012), Adolf Wagner explains that government spending and policies develop from time to time. The increasingly expanding role of the state in the economic and social life of society as a whole is the core of his theory. Wagner explained that in an economy where for every increase in income, government spending also increases proportionally, this is because the state needs to manage the relationships that occur in the eyes of the public, law, schools, entertainment, culture, and so on. Government spending increased for a variety of reasons, including the expansion of banking activities and development, the expansion of welfare functions, and the expansion of defense and security functions, according to Wagner's theory. The "Organic Theory of State", which assumes that the government is an individual with the freedom to act independently of other societies, is the basis of Wagner's theory (Mankiw, 2012).

Government spending is expenditure or expenditure intended for the public interest in growing the regional economy and improving the ability of the community. Government spending is prioritized in improving and protecting the quality of life of the community as a mandatory fulfillment for the region through the improvement of health, education, public and social facilities, basic services and the development of social security as stipulated in Law Number 32 of 2004. Nurmainah (2013) stated that the role of government spending in developing countries is significant because of the limited role of the private sector in the economy, therefore in this case the role of the government is very important.

Government expenditure for the education function is in accordance with the Regulation of the Minister of Finance of the Republic of Indonesia Number 84/PMK.7/2009 concerning the Allocation of the Education Function Budget in the Regional Revenue and Expenditure Budget which explains that education expenditure is a budget allocation for education financing which is the responsibility of the government. The determination of the allocation is at least 20% of all APBD spending. The allocation of health expenditure is implied in Law Number 36 of 2009 concerning Health which explains that the allocation for health is 5% outside the salary from the State Budget, for city/district and provincial governments, it is 10% outside the salary from the APBD. Regulation of the Minister of Finance of the Republic of Indonesia Number 101/PMK. 02/2011 also explains several types of budgets from health functions which include individual health services, health supplies, family planning, and health research and development.

Government expenditure for economic functions in relation to regional development is aimed at realizing regional economic development. One of the

economic functions of government spending is infrastructure spending. Infrastructure has three important roles for economic integration, namely: first, the availability of infrastructure is a trigger for economic growth. Second, the available infrastructure network is very important in the smooth running of investment and trade activities. Third, to overcome the inequality of economic development between regions. Good infrastructure is able to facilitate economic mobility between regions/regions so that it can attract investors to invest in the regions and have an impact on the creation of job opportunities and improvement of development conditions. Increasing development conditions will have an impact on poverty alleviation and increasing people's welfare.

The Endogenous Growth Theory put forward by Romer, P. M. (1990) argues that long-term economic growth is driven by internal economic factors, especially investment in human resources, innovation, and technology. Government spending on education, research, and infrastructure plays a crucial role in driving these growth drivers. By focusing on inclusive policies that increase opportunities for all community groups, especially disadvantaged groups, government spending can encourage inclusive economic development.

Inclusive Economic Development IDDC (International Disability and Transparency Consortium) defines inclusive economic development as a process to ensure that all socially underrepresented groups can participate fully in the development process. Kanbur & Rauniyar (2010) said that improvements are comprehensive when all residents participate and the delivery is in accordance with the cycle, regardless of the conditions or individual foundations.

The Capability Approach (1999) put forward by Amartya Sen is one of the most influential theories underlying inclusive development. Sen argues that development should be seen as a process of expanding the real freedom that every individual enjoys. According to Sen, development focuses not only on economic growth but also on improving people's abilities such as access to education, health services, and basic rights that are essential for living a life they cherish. In the context of inclusive development, this theory highlights the importance of ensuring that all individuals have the ability to participate and benefit from economic opportunities.

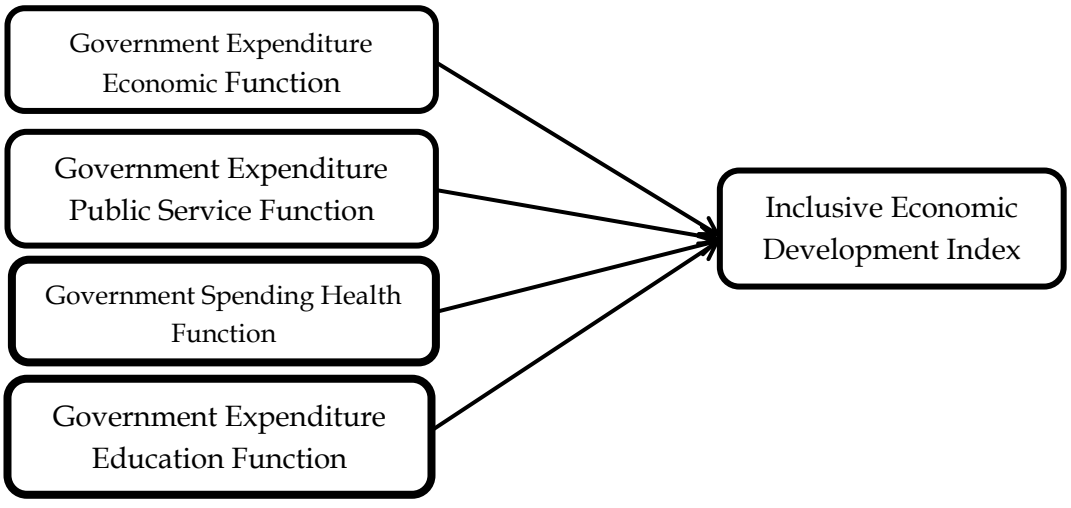
Warsilah (2015) conducted research on inclusive economic development. According to his findings, the inclusive development strategy is a component of the implementation of strategies based on social aspects of development and responses to reduce marginalization. Poor development management is also based on the idea that growth or progress of the economy should be purely the goal. By involving city residents in the urban development process, his research in Solo shows that a participatory building approach can reduce social exclusion and encourage social inclusion.

IPEI is one of the measuring tools to monitor the level of growth and development inclusivity at the district/city, provincial, and national levels in Indonesia. Measuring inclusivity by looking at aspects of economic growth, aspects of poverty, inequality, as well as aspects of opportunity and access. The index is formed from 21 indicators, 8 sub-pillars, and 3 pillars.

Previous Research

According to research by Fitrianasari (2021), there is a positive and significant influence between the variables of expenditure for health services and the importance of education with the inclusive economic development index. Sihombing (2023) also carried out a similar study, and the findings show that expenditures made for education and health care functions have a positive and significant impact on IPEI. Purwanti & Rahmawati (2021) in their research also explained that the functions of education and health have a significant impact on inclusive economic growth. Sri Hartati (2021) According to the findings of her study, education and health spending factors on the part of the government have a major impact on the development of an inclusive economy. According to the findings of Arrfah and Syafri (2022), the variable of expenditure on the health function has a positive and significant influence, but the variable of expenditure on the education function has a positive but not significant influence. This explains that spending on health functions has a greater impact on inclusive growth than spending on education functions. Safitri (2021) explained that government expenditure on health and education functions has a positive and significant impact on the inclusive economic development index, as well as in the short or long term. According to research by Yasni & Muhammad (2020), expenditure on the education function is not only negative for economic development in the short term, but in the long term has a significant impact on economic growth. And with regard to health functions, both short-term and long-term government spending have a positive but not significant relationship for economic growth.

Theoritical Framework



METHODOLOGY

This study is about the influence of government expenditure from the variables of economic functions, public services, health and education on the Inclusive Economic Development Index with the selected time period in 2016 – 2023. The area in this study is in all provinces on the island of Sumatra with the provinces of Aceh, North Sumatra, West Sumatra, Riau, Riau Islands, Jambi,

Bengkulu, South Sumatra, Bangka Belitung Islands, and Lampung. This study uses the Panel Data Regression Analysis method. The type of data used in this study is quantitative descriptive. The data sources used are secondary data obtained from the Directorate General of Fiscal Financing (DJPK) of the Ministry of Finance (2023) and Bappenas. The best model selection test was used in this study consisting of a normality test, a multicholineartias test, a chow test, and a hausman test. The statistical tests used are the t-test, and R2 to determine the influence of independent variables on dependent variables simultaneously or partially. The following equations from the regression of panel data in this study are:

The models or functions that will be used are:

$$Y_t = a + \beta_1 X_1 it + \beta_2 X_{2it} + \beta_3 X_{3it} + \beta_4 X_{4it} + \varepsilon_t$$

Information:
X_1 : government expenditure economic function
X_2 : Government expenditure on public service functions
X_3 : government expenditure health function
X_4 : Government expenditure on the education function
a : Constant
$\beta_{1...4}$: Regression coefficient of each independent variable
Q: Research period (2016-2023)
ε : disruptor variable

RESEARCH RESULTS

Analysis of Classical Assumptions

Classical assumption test used in this study is the normality test and multicolinearty test.

a. Normality Test

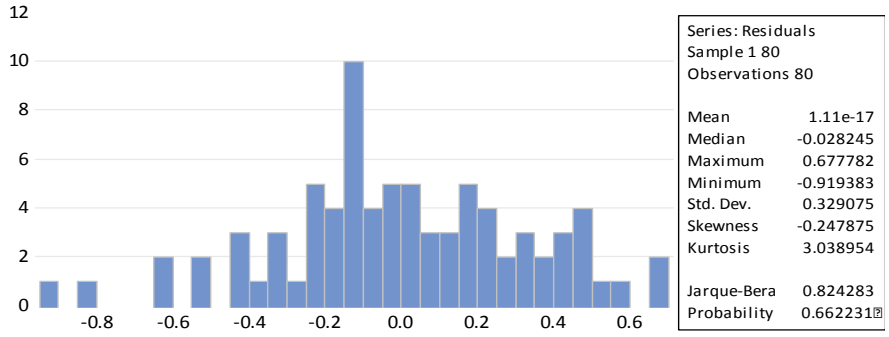


Figure 2 Normality Test

Based on Figure 1.3, it can be seen that the probability value is 0.662 > 0.05, so it can be concluded that the data is normally distributed.

b. Multicolinearity Test

Table 1 Multikolinearity Test

	X1	X2	X3	X4
Economic Functions	1.000000	0.408659	0.636090	0.561486
Public service functions	0.408659	1.000000	0.360272	0.501738
Health Function	0.636090	0.360272	1.000000	0.623915
Educational Function	0.561486	0.501738	0.623915	1.000000

Based on Table 1.3, it can be seen that each variable has a collinearity value in each relationship has a value of 0.000<1 so that no symptoms of Multicolinearity.

Model Selection Analysis

To find out how the influence of government expenditure by using variables of economic functions, public services, health and education on the Inclusive Economic Development Index on the island of Sumatra in 2016 - 2023 by using the panel data regression method which has three models used including the common effects, fixed effects, and random effects models. To choose which regression model is in accordance with this study, it can be done by using the CHOW Test, and the Hausman test. The results of the Chow test are to determine which regression model is more appropriate to use, whether the common effects or fixed effects model. Meanwhile, the Hausman test is carried out to determine which regression model is more appropriate to use, whether the random effects or fixed effects model is carried out to determine which regression model is more appropriate, whether common effects or random effects.

Chow Test

Table 2 CHOW Test

Effects Test	Statistic	d.f.	Prob.
Cross-section F	7.663815	(10,65)	0.0000
Cross-section Chi-square	62.311064	10	0.0000

The analysis showed that the probability value of F for the likelihood ratio comparison test in this model is very low, namely 0.0000 which is much more large the alpha value is 0.05. Therefore, the null hypothesis (H0) accepted alternative hypothesis (H1) rejected. Based on these results, it can be concluded that the model that best suits the data is the model with Fixed Effects.

Hausman Test

Table 3 Hausman Test

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	4.944319	4	0.2931

Based on the results of the hausman test, the random effect model vs the fixed effect model above, the probability value of chi-square Random 0.2931> 0.05 is obtained, then the selected model is the Random Effect Model (REM) model is a more appropriate model to use.

Table 4 Results of Regression Data Panel Random Effect Model (REM).

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	5.890030	0.147474	39.93938	0.0000
Economic Function	8.67E-14	7.19E-14	1.206344	0.2315
Public Service Function	-7.80E-15	2.29E-14	-0.341113	0.7340
Health Function	3.46E-13	1.54E-13	2.249111	0.0274
Education Function	7.16E-14	3.24E-14	2.208408	0.0303

Mean dependent var	1.838988	R-squared Adjusted	0.622246
S.D. dependent var	0.325235	R- squared	0.042729
Sum squ ared resid	4.572269	S.E. of regression	0.246908
Durbin-Watson stat	1.881867	F-statistic	1.881571
		Prob(F-statistic)	0.012246

Regression Equation

Y= 5.89 + 8.67 X1 + -7.80 X2 + 3.46 X3 + 7.16 X4

Hypothesis Test

Coefficient of Determination

Based on Table 4 shows the magnitude of the coefficient of determination R Squared = 0.62, meaning variable function economy, public service, health and education affect inclusive economy between provinces on the island of Sumatra the remaining 0.62 or 62% is influenced by other variables that are not included in this research model.

F Test

Known F-statistic value of 1881 with the value of Prob. (F-statistic) of 0.012 < 0.05 then the bias drawn the conclusion that the independent variable (X) significant effect simultaneously (simultaneously) to the dependent variable (Y).

T Test

Statistical test for economic function variables probability is 0.231 > 0.05 which means H1 is rejected, thus accepting H0 which can be interpreted statistically economic function does not have a significant effect, but is directed positively towards the index of Inclusive Economic Development on the island of Sumatra. Furthermore, the coefficient value is 8.670%. This shows that every 1% increase in economic function will affect the inclusive economic development index of 8,670. Because it is positive, the economic function and the Inclusive Economic Development Index are interconnected.

Statistical test for service function variable probability is 0.734 > 0.05 which means H1 is rejected, thus receiving H0 which can be interpreted statistically public service function has no significant effect and negative direction on the index of Inclusive Economic Development on the island of Sumatra. Furthermore, the coefficient value is -7.800%. Thus, if the health function increases by 1% , The Inclusive Economic Development Index will decrease by 7,800%.

Statistical test for health variables probability is 0.027 < 0.05 which means H0 is rejected and H1 is accepted which can be interpreted statistically health function has a significant effect and positive direction on the index of Inclusive Economic Development on the island of Sumatra. Furthermore, for the value of the coefficient is equal to -3.460. Thus, if the health function increases by 1% , The Inclusive Economic Development Index will decrease by 3,460%

Statistical test for education variable probability 0.030 < 0.05 which means H0 rejected and H1 accepted which can be interpreted statistically the function of Education has a significant and positive effect on the index of Inclusive Economic Development on the island of Sumatra. Furthermore, the coefficient value is equal to 7.160. Thus, if the educational function increases by 1%, The Inclusive Economic Development Index will increase by 7,160%.

DISCUSSION

Economic function variables showed positive directional results are not significant to IPEI with a regression coefficient of 8,670. This shows that if government spending on economic functions increases, IPEI also increases by 8,670 assuming other variables remain. This influence is in line with faizin and Prabowo's (2022) research in which the IPEI of growth aspects is not influenced by the expenditure of economic functions. While according to Safitri (2021) in the long term IPEI is influenced by spending on economic functions positively and significantly. This may indicate that government spending on economic functions has not been fully felt by the wider community.

One form of government spending is the economic function of infrastructure. So that the benefits of government spending on economic functions can be better Felt by the wider community, one of them should be focused on infrastructure development whose usefulness can be enjoyed directly or in the long term by the wider community. The development of the infrastructure itself will definitely require more labor that will open up new jobs which will ultimately have an impact on the builders of an cyclical economy.

In addition, the expenditure of this economic function is also associated with MSMEs, namely where there is a principle of empowerment in it. The empowerment creates equity and has an impact on the achievement of inclusive economic development. On the theory of "Wagner" also explained that the amount of government spending and economic development have a positive relationship in infrastructure development. Government spending on economic functions in the long term should be directed to the quality of spending to accelerate infrastructure development and the government should support the strengthening of infrastructure and connectivity between regions, as well as the quality of spending to improve the quality of expenditure allocation of economic functions in the Kur (people's Business Credit) program.

General service function variables showed negative directional results were not significant to IPEI with a regression coefficient of -7,800. This shows that if the expenditure of government functions generally increases, IPEI will decrease by 7,800%. It is contrary to the initial hypothesis that spending on public service functions in this sector will be positive and directed towards inclusive economic development. Several factors can be used to explain this finding. First, according to Tanzi's (1998) theory of fiscal corruption, lack of efficiency in allocating and executing public budgets can lead to worse government spending. Corruption and inefficient bureaucracies often reduce the benefits of public spending, especially in critical sectors on which Inclusive Development is based, such as education and health. Projects that are not productivity-oriented often absorb public spending that would otherwise focus on improving the quality of public services.

Second, other inhibiting factors include geographic inequality and development imbalances throughout Sumatra. As explained by Rodríguez-Pose and Ezcurra (2010), more developed areas such as North Sumatra tend to receive larger budget allocations compared to more remote areas such as Aceh, Jambi, or South Sumatra. Government spending does not support inclusive development equally because of this inequality in budget distribution.

Third, research by Dabla-Norris et al. (2012) highlighting that the effectiveness of public spending depends largely on the quality of institutions. If local institutions are unable to manage budgets properly, government spending directed at public services will not be able to achieve optimal results in promoting inclusive growth. To improve the quality of public institutions and ensure a more equitable distribution of budgets between developed and underdeveloped regions on the island of Sumatra, the government should consider improving the monitoring and evaluation system of public budget allocations. It is also important to increase the effectiveness of spending on public services sector.

Health function variables showed a significant and positive effect on IPEI with a regression coefficient of 3,460. This shows that if the expenditure of government health functions increases, IPEI will increase by 3,460% through constant expectation of other variables. This influence is in line with research carried out by Arrfah & Syafri (2022) and Sihombing (2023), in their research

showing that government spending on health functions has a significant positive impact on IPEI.

This is in line with Wagner's theory, which states that government spending increases due to interactions in society through improvements in health levels. Health I a critical element in the direction of inclusive economic growth. In Law No. 6 of 2009, it is explained that the purpose of development in the field of Health is to increase the willingness, ability, and awareness of each individual to live a healthy life. Thus, it is expected that the level of Public Health in general will increase, followed by the increase in inclusive economic growth.

Health is a long-term investment and the country is aware of the importance of the role of health as a major force for the advancement of economic growth, one of which is the National Health Insurance program (JKN). JKN is one of the forms of National Social Security contained in Law Number 40 of 2004. This is related to the sub-pillars of the Inclusive Economic Development Index, which can be seen from the percentage of the number of people who have health insurance that increases every year. The higher the number of people who have health insurance, especially the poor, the realization of equitable economic development that is more inclusive.

As for what the government should do to achieve the effect of government spending on health functions for inclusive development in the long term, including: (1) the quality of spending to strengthen the superior Generation program through training for medical personnel and (2) the quality of spending to improve the quality of Service and effectiveness of JKN, adjustment and validity of data to be on target. From these implications, it is expected that the National Health System will be good so that the welfare of the community will be high. High public welfare will have an impact on high community productivity, so that optimal inclusive development will be achieved in the long term.

The educational function variable showed significant positive directional results on the Inclusive Economic Development Index with a numerical regression coefficient of 7.160. this shows that if government spending on education increases, IPEI tends to increase by 7,160% through the assumption that other variables are constant. This influence is in line with the research carried out by Hartati (2021) and Fitria nasari (2021), both of which both have IPEI results positively and significantly influenced by government spending on education aspects.

Economic growth and government spending if associated with the theory and research results have a relationship that supports the theory of "Keynes" where economic growth and government spending have a positive relationship. It was described at length by Keynes in the General Theory Keynes which explains that government spending spurred economic growth. Keynes explained that increased government spending can encourage increased aggregate demand followed by increased production of goods and services so that economic growth will also increase. Government spending in this case is seen as an exogenous force that alters *output* aggregate

Spending on educational functions is a very important investment for economic growth in a more inclusive direction. Education is part of *public service* from the state to its people. With this, the government is aware of the importance of the role of education as a major force for the advancement of more inclusive economic growth. Therefore, the expenditure on educational functions is budgeted higher than other expenditures. But it takes enough time to achieve a decent education and be able to compete.

The government focuses more on the 12-year compulsory education policy which is a government program and is listed in the 2014-2019 RPJMD. Meier & Rauch (2000) explain about the high government spending in the education sector will affect the development of Education which can be seen from the increasing number of students who finish school. This turns out to be related to the sub-pillar of the Inclusive Economic Development Index, namely the old school expectation rate which increases every year.

CONCLUSION AND RECOMMENDATION

Based on the results and discussion of research that has been done on the effect of government spending on the index of inclusive economic development on the island of Sumatra, it was concluded that the variable economic function does not have a significant effect on the index of inclusive economic development on the island of Sumatra. Variable function of public services does not have a significant and negative effect on the Inclusive Economic Development Index, which means that any increase in the function of public services will reduce the index of Inclusive Economic Development in Sumatra. While the health function variables have a positive and significant effect on the index of inclusive economic development on the island of Sumatra. Educational variables have a positive and significant effect on the index of economic development on the island of Sumatra. This means that every improvement in health and education functions leads to a higher index of inclusive economic development on the island of Sumatra.

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