International Journal of Economic Research

ISSN : 0972-9380

available at http: www.serialsjournals.com

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Volume 14 • Number 17 • 2017

The Analysis of the Effects of Capital Expenditure and Human Development Index on Economic Growth and Poverty in East Aceh Regency

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Abstract: The purpose of this study is to analyze the effects of capital expenditure of local government and of human development index, both partially and simultaneously on economic growth and poverty.The capital expenditure of local government and human development index as the exogenous variables and economic growth and human development index as the endogenous variables. This study used the time-series data with a time series of 2005-2015. The analysis was conducted by using the path analysis method using Eviews program. The results with a significance level of 5% showed that, simultaneously, the capital expenditure and human development index had significant effects on economic growth and simultaneously the capital expenditure and human development index had significant effects on poverty through economic growth. Partially, capital expenditure had a positive and significant effect on economic growth, while the human development index had a negative and significant effect on economic growth. Then, partially, the capital expenditure had a positive and insignificant effect on poverty and human development index had a negative and insignificant effect on economic growth.

Keywords: Capital Expenditure, Human Development Index, Economic Growth, Poverty.

JEL Classification Codes: E22, O15M, O47, P36

1. INTRODUCTION

The implementation of regional autonomy has given authority to regions to regulate and manage their own local governments. It is conducted in order to realize the demands of society effectively and efficiently in order to realize the common prosperity. Common prosperity can be realized if the local governments provide services to the community through the programs such as increasing human capital, the availability of adequate infrastructure and sufficient employment. The availability of adequate infrastructure such as educational facilities and healthcare facilities can improve the Human Development Index (HDI). HDI is

one of the important factors in the performance of the regional economy which is expected to encourage economic growth in the long term, so that the impact can be perceived by the community. A successful economic performance is characterized by the increasing productivity and income per capita of the community, so that the prosperity as the main goal of development will be achieved (Muda*et al.*, 2017).East Aceh is one of the regencies in Aceh Province. Since 2000, East Aceh had experienced an expansion which was aimed at having equitable regional development. The newly created regions from East Aceh Regency are Langsa City and Aceh Tamiang Regency. In order to realize the equitable regional development there is a need of budget that can be used as public expenditure such as capital expenditure (Yahya*et al.*, 2017).The capital expenditure in Kabupaten Aceh Timur fluctuates every year. The development of capital expenditure in 2007-2015 ranged from -19% to 200%. Fluctuation in capital expenditure was due to the fluctuation in direct expenditure which is composed of goods and services expenditure and government personnel expenditures which resulted in fluctuation in capital expenditure every year.United Nations Development Program (UNDP), is a program that develops the measurement of development performance named Human Development Index (HDI). The Regional Bureau Statistics (BPS) of Aceh,stated that the indicators used for developing HDI are life expectancy, literacy rate and the real per capita income based on the purchasing power parity (PPP). East Aceh was one of the regencies that had the lowest position in the period of 2010-2015. East Aceh District was consistently ranked 18th for HDI in that period.

High economic growth becomes one of the priorities of development of a country, which is one of the indicators of successful development. The economic growth rate of East Aceh Regency in the period of 2007-2015 fluctuated between 3% and 5%. Poverty will have a negative impact which obstructs the process of regional development. Poverty is the inability of the population to meet the minimum standards of basic needs which include food and non-food needs. In order to measure the poverty rate, the Central Bureau of Statistics (BPS) uses the concept of basic needs approach. The development of the number of poor people in East Aceh Regency in the period of 2007-2015 fluctuated between -0,65% to -10%. The decline in poverty rate illustrates the improvement of community welfare in East Aceh Regency.

2. THEORITICAL REVIEW

2.1. Capital Expenditure

In the Government Regulation No. 58 of 2005, it is stated that capital expenditure is any spending on the purchase/procurement of fixed and other assets that have a useful life of more than 12 (twelve) months for the use in government activities, such as land, equipment and machineries, buildings, networks, books for library, and animals. In the Regulation of the Minister of Home Affairs No. 13 of 2006, capital expenditure is defined as any spending on the framework of purchasing/procuring or constructing of the tangible fixed assets that have a useful life of more than 12 (twelve) months for the use in government activities, such as land, equipment and machineries, buildings, roads, irrigation and networks, and other fixed assets.

According to Government Regulation No. 71 of 2010, capital expenditure is any spending of Local Government with a useful life of more than 1 fiscal year and will increase the assets or wealth of the region and will then add routine expenditure such as maintenance cost to the operational expenditure group. Capital expenditure is used for acquire local government fixed assets such as equipment, infrastructure and other fixed assets (Muda *et al.*, 2017). The capital expenditure is acquired by buying through auction or tender process.

Sularso and Restianto (2011) and Yahya *et al.*, (2017) stated that the allocation of capital expenditure is the allocation of budget expenditure for the acquisition of the fixed and other assets that provide benefits for more than one accounting period, compared to total expenditure in the Regional Budget (APBD). The development of facilities and infrastructure by the local government has a positive effect on economic growth (Kuncoro, 2004). The fundamental requirement for economic development is the level of procurement of development capital that is balanced with population growth. The increasing infrastructure and improvements by local governments are expected to encourage regional economic growth.

2.2. Human Development Index (HDI)

The Human Development Index was firstly introduced in 1990 by one of the international organizations of the United Nations, namely UNDP (United Nation Development Programme).The methodology of HDI calculation had changed over years. In 1990, it was firstly introduced: the HDI components used were AHH (life expectancy), AMH (literacy rate), GDP per capita (Arsa, 2014). Aggregation with arithmetic average. In 1991, there were some changes made in terms of improvements: the HDI components used were AHH (life expectancy), AMH (literacy rate), RLS (average school length) and GDP per capita. Furthermore, in 1995, there were some improvements made: the HDI components used were AHH (life expectancy), AMH (literacy rate), APK combination (gross participation rate) and GDP per capita. In 2010, in terms of completion: the HDI components used were AHH (life expectancy), AMH (literacy rate), APK combination (gross participation rate) and GDP per capita. In 2011, in terms of completion: the replacement of base year of GNP per capita from 2008 to 2005. Then, in 2014, in terms of completion: the replacement of base year of GNP per capita from 2005 to 2011, the change in the educational index aggregation method from geometric average into arithmetic average.According to Brata (2002), the relatively high level of human development will affect the economic performance through the capability of the population and the consequence in the form of improved productivity and creativity of the community. With the improved productivity and creativity, the people can obtain and manage the resources that are essential for economic growth.

2.3. Economic Growth

In general, economic growth is defined as an improvement in the ability of an economy to produce goods and services. Economic growth is one of the most important indicators in analyzing the economic development of a country (Mankiw, 2006). Economic growth indicates the extent to which economic activity will generate additional income for the community in a certain period (Sirojuzilam *et al.*, 2016; Tarmizi *et al.*, 2016 and Tarmizi *et al.*, 2017). Sularso and Restianto (2011) state that regional economic growth is an increase of (GDP) or GRDP regardless of whether the increase is greater or less than the rate of population growth or whether there is any change in economic structure or not. GDP growth rate is the rate of growth from year to year which is calculated by the following formula: (Gustav, 2004).

$$GRDP\,Growth\,Rate\,(G) = \frac{GRDPt - GRDPt-1}{GRDPt-1} \times 100$$

According Jhingan (2004); Muda *et al.*, (2016 & 2017), the process of economic growth is influenced by two factors, namely economic and non-economic factors. Some economic factors that have some effect on economic growth are natural resources, capital accumulation, human resources, technological advancement and the classification of working hours and production scale. The non-economic factors

collectively have some effects on the economic progress of each other. Therefore, the non-economic factors also have an important meaning in the economic growth. Some non-economic factors are social, organizational and political, and administrative factors.

2.4. Poverty

Theories of poverty generally lead to two major paradigms that also have some effect on the comprehension on poverty and poverty alleviation. These two paradigms have a very clear distinction, especially for viewing poverty and providing solutions regading poverty (Sadalia *et al.*, 2017). The paradigms mentioned above are as follows:

2.4.1. Neo-Liberal Paradigm

According to Muthalib (2015), the neo-liberal theory is rooted in a classical political work written by Thomas Hobbes, John Lock and John Stuart Mill which essentially states that an important component of a community is individual freedom. In the field of economics, according to the monumental work of Adam Smith, *the Wealth of Nation,* it is seen as a reference of the neo-liberal who put forward *laissez faire*principle as idea favoring the free-market mechanism. In general, the neo-liberal supporters argue that poverty is an individual issue caused by the individual's weakness(es) or choice(s). Poverty will be reduced by itself if the market forces are expanded to the greatest extent and economic growth is driven to as high as possible. Directly, poverty reduction strategies must be *residual* and involve only families, independent groups or religious institutions and the role of government should be non-existent. The implementation of Social Security Network (JPS) programs in some countries is a concrete example of the neo-liberal effect in poverty alleviation. Thus, the neo-liberal people perceive that the institutionalized strategies of poverty alleviation are considered as uneconomic actions and result in dependency.

2.4.2. Social Democracy Theory

Social democracy theory sees that poverty is not an individual, but a structural issue (Todaro, 2011). Poverty is caused by unfairness and inequality in the society due to the obstructed access for certain groups to various sources of society (Tarmizi *et al.*, 2017). The theory that has a basis on the mixed economic principles and Keynesian economic management emerged as a response to the economic depression that occurred in the 1920s and early 1930s. According to the social democratic view, the strategy of poverty should be institutionalized. The social security and social assistance programs adopted in the United States, Western Europe and Japan are the examples of anti-poverty strategy characterized by social democratic theory. Social security in the form of income allowances or pension funds, for example, can improve independency because it can provide the basic income that people will have the ability to meet their needs and make choices. Conversely, the absence of such basic services can lead to dependence because it can make people unable to meet their needs and make choices. Thus, those who support the social democracy believe that residual, short-term project-oriented poverty is a money-spending strategy because the effect is also short-term, limited and is not oriented to empowerment and sustainability (Muthalib, 2015).

2.5. Previous Studies

Nurmainah (2013) conducted a research entitled "The Analysis of the Effect of Local Government Capital Expenditure, Employment and Human Development Index on Economic Growth and Poverty (A Case

Study on 35 Regencies/Municipalities in Central Java Province)". The purpose of this study was to examine the effect of local government capital expenditure, employment and human development index on economic growth and poverty on 35 regencies/municipalities in Central Java Province. This study used secondary data. There were local government capital expenditure, employment and human development index as exogenous variables, and economic growth and poverty rate as endogenous variables. This study used panel data that combined the time-series and cross-sectional data. The data were analyzed by using *structural equation modeling* (SEM). The results showed that the four proposed hypotheses were accepted and a hypothesis was rejected. Hypothesis 1 states that local government capital expenditure has a significant and positive effect on economic growth. Hypothesis 2 states that the labor employment has a positive and significant effect on economic growth. Hypothesis 3 states that the human development index has a positive and significant effect on economic growth. Hypothesis 4 states that economic growth has no significant effect on poverty. Hypothesis 5 shows that the human development index has a significant negative effect on poverty.

Kotambunan, *et al.,* (2016) conducted a study entitled "The Analysis of the Effect of Capital Expenditure and Human Development Index on Poverty in North Sulawesi Province (In 2005-2014)". The purpose of this research was to analyze the effect of capital expenditure and human development index on poverty in North Sulawesi. Data analysis method used in this research was the *Ordinary Least Square* (OLS) with multiple linear regression model which was facilitated by Eviews 8.0 program. The results showed that capital expenditure has a positive and significant effect on poverty. Then, the human development index has a negative and significant effect on poverty.

3. RESEARCH METHODS

Exploratory research is fundamental and aims to obtain information, information, data about things that have not been known (Dalimun the *et al*., 2016 & Nurzaimah *et al*., 2016). Exploratory research is a study that aims to test a theory or hypothesis to strengthen or even reject the theory or hypothesis of existing research results.Exploratory research does not require a certain hypothesis or theory (Gusnardi *et al*., 2016)The scope of this study was a study on public economy with the variables of local government capital expenditure, human development index, economic growth and poverty. This study was conducted by using the secondary data *(time-series)* in the period of 2005-2015. The data were collected by using direct observation technique that was collecting the data of Capital Expenditure from the Regional Asset Management Financial (DPKAD) office of East Aceh Regency and the data of HDI, Product Domestic Regional Bruto (PDRB) and Poverty rate in 2005-2015 which were available at the The Regional Bureau Statistics of East Aceh Regency.

In order to meet the objectives in this study and to test the hypotheses that had been determined, the *path analysis* was then conducted. Path analysis is actually an extension of multiple linier regression analysis. This method was used because the effects which wanted to be observed had the principle of *mutual simultaneous shaping* as a substitute for causality which is an effort to explain the interrelated factors that exist in the problem. The path analysis aims at showing the direct and indirect effect of a set of exogenous variables on endogenous variables by calculating the path coefficient. The path coefficient represents the degree of direct effect of the independent variable on the dependent variable.The following figure can show a full structure for theses two equations, in order to see the relationship between independent variables and the dependent variable.

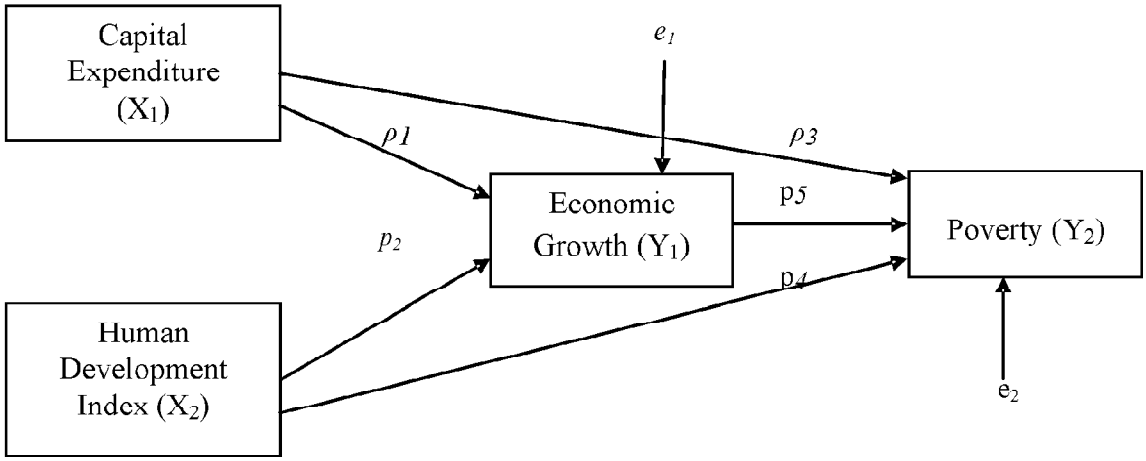

Figure 1: Full Structural Model

Based on Figure 1, in order to find out the relationship pattern of relationship of each variable, it can be arranged for an equation system of the sub-structure, which is: the equation of sub structure 1 as follow:

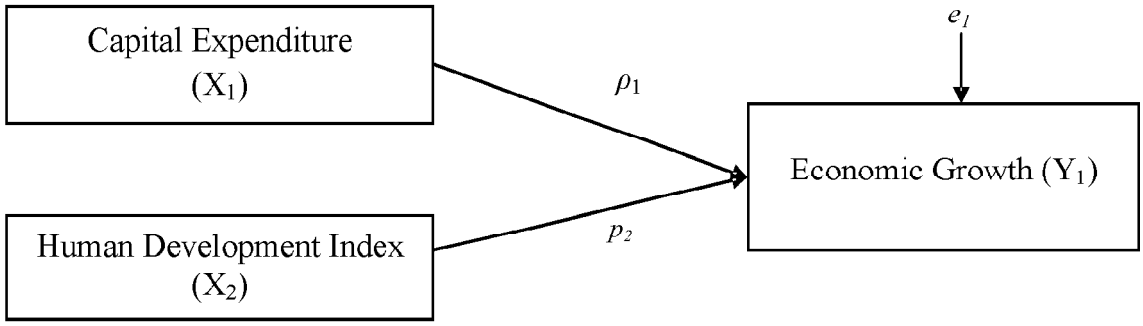

Figure 2: Sub-structure 1

The equation of sub-structure 1 in Figure 2 describes that the effect of capital expenditure and human development index on economic growth with the following equation:

$$Y_1 = \rho_1 X_1 + \rho_2 X_2 + e_1$$

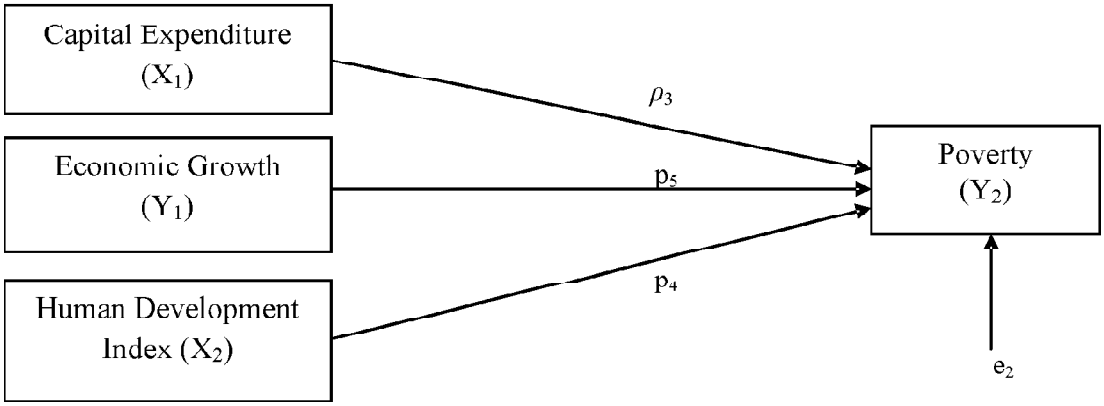

Figure 3: Sub-structure 2

The equation of sub-structure 2 in Figure 3 describes the effect of capital expenditure and human development index on poverty with the following equation:

$$Y_2 = \rho_3 X_1 + \rho_4 X_2 + \rho_5 Y_1 + e_2$$

4. RESULTS AND DISCUSSION

4.1. Results

Based on the results of the analysis of panel data for the equation of sub-structure 1, the path coefficients were obtained as follows:

$$Y_1 = 3{,}27E\text{-}06X_1 - 104676{,}6X_2 + 0{,}4559\ e$$

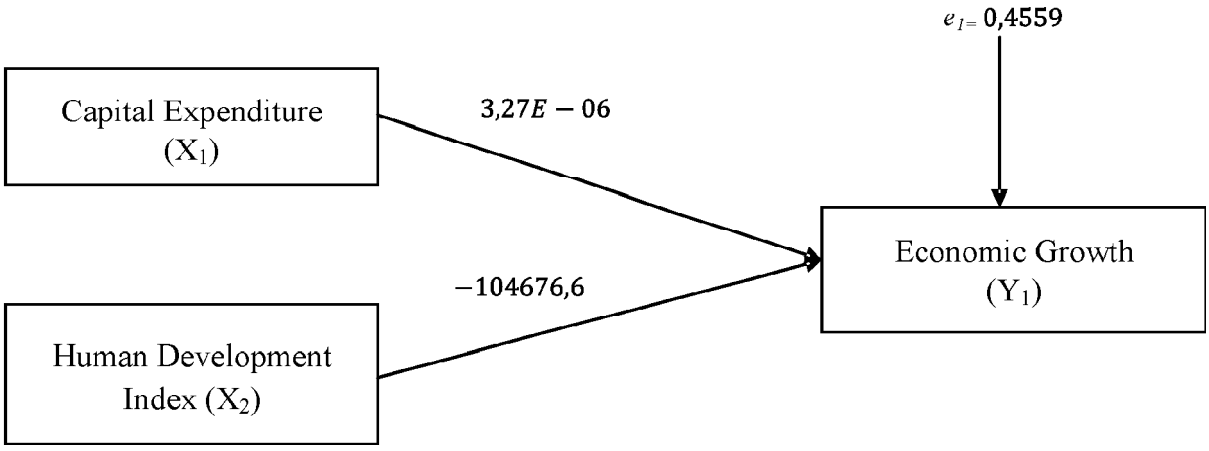

Figure 4: The Path Coefficients of the Equation of Sub-Structure I

Then, based on the results of the analysis of panel data for the equation of sub-structure 2, the path coefficients were obtained as follows:

$$Y_2 = 2{,}10E\text{-}08\ X_1 - 1713{,}732\ X_2 - 0{,}022854\ Y_1 + 0{,}4144\ e$$

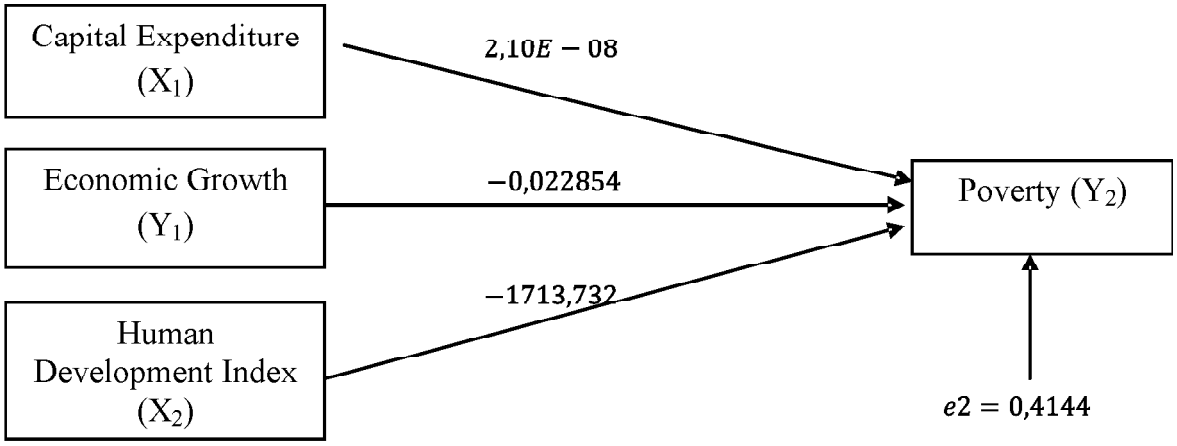

Figure 5: The Path Coefficients of the Equation of Sub-Structure 1

Meanwhile, the effect of the relationship of each variable can be illustrated as follow:

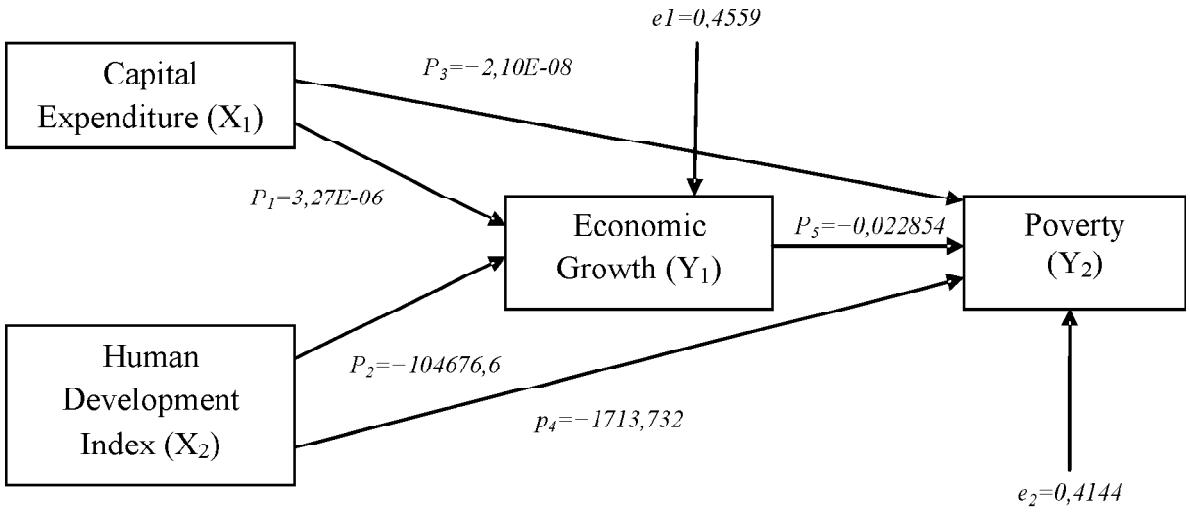

Figure 6: The Relationship of Path Coefficients of the Research Model

The coefficient of determination $R^2$is a value (proportional value) which measures the ability of the independent variables used in the regression equation in explaining the dependent variables (Gujarati, 2003). The value of coefficient of determination ranging between 0 and 1. The small value of coefficient of determination R^2 (near 0) means that the ability of the independent variables is very limited simultaneously in explaining the dependent variables. The value of coefficient of determination R^2 which is near to 1 means that the independent variables give almost all information needed to predict the variation of dependent variables.

Table 1
The Regression Analysis of the Equation of Sub-structure I

Variable	*Coefficient*	*Std. Error*	*t-Statistic*	*Prob.*
BM	3.27E-06	1.02E-06	3.203662	0.0125
IPM	-104676.6	38692.20	-2.705368	0.0268
C	11872928	2696827.	4.402555	0.0023
R-squared	0.792106	Mean dependent var		5403880.
Adjusted R-squared	0.740133	S.D. dependent var		692672.9
S.E. of regression	353105.0	Akaike info criterion		28.61392
Sum squared resid	9.97E+11	Schwarz criterion		28.72244
Log likelihood	-154.3766	Hannan-Quinn criter.		28.54551
F-statistic	15.24060	Durbin-Watson stat		0.929619
Prob (F-statistic)	0.001868			

Source: Research Result, 2017 (processed data).

The coefficient of determination for the equation of sub-structure I can be seen in Tabel1, that R^2 = 0,792106. It means that all independent variables, capital expenditure and human development index,

have an effect on economic growth variable for 79,21%, while the rest 20,79% are affected by other factors. The *error*value for the equation of sub-structure 1 is $\sqrt{1-0,792106} = 0,4559$.

Table 2
The Regression Analysis of the Equation of Sub-structure II

Variable	*Coefficient*	*Std. Error*	*t-Statistic*	*Prob.*
BM	2.10E-08	2.50E-08	0.839710	0.4288
IPM	-1713.732	869.1706	-1.971686	0.0893
PE	-0.022854	0.005739	-3.981888	0.0053
C	308392.0	80994.53	3.807566	0.0066
R-squared	0.828225	Mean dependent var		73081.82
Adjusted R-squared	0.754608	S.D. dependent var		11571.37
S.E. of regression	5732.118	Akaike info criterion		20.42085
Sum squared resid	2.30E+08	Schwarz criterion		20.56553
Log likelihood	-108.3146	Hannan-Quinn criter.		20.32964
F-statistic	11.25036	Durbin-Watson stat		1.342467
Prob(F-statistic)	0.004552			

Source: Research Result, 2017 (processed data).

Then, in Tabel 2, the coefficient of determination R^2 is in the R-Squared column. It was known that the coefficient of determination $R^2 = 0,828225$. It means that all independent variables, capital expenditure and human development index, have an effect on poverty for 82,82%, while the rest 17,18% are affected by other factors. The error value for the equation of sub-structure 2 is $\sqrt{1-0,828225} = 0,4144$.

4.2. Results and Discussion

4.2.1. The Effect of Capital Expenditure and Human Development Index on Economic Growth

Based on the results of hypothesis test in this study, it was proved that, simultaneously, the effect of capital expenditure and human development index variables on economic growth was significant with F statistics and prob 0,001868 or less than 0,05. Then, the value of coefficient of determination (R2) R-Squared was obtained for 0,792106 which can explain that the independent variables consist of capital expenditure and human development index had an effect on economic growth variable of 79,21%, while the rest 20,79% explained by other variables which were not included in the estimation of this study. Thus, the first hypothesis states that there is a simultaneous effect between capital expenditure and human development index variables on economic growth.The results of this study explained that there is an effect of capital expenditure and human development index on economic growth and this is in accordance with the research conducted by Lestari and Fitrayati (2011), where the research variables consisted of capital expenditure and human development index had simultaneous effect on economic growth. The capital goods such as factories, machineries and equipment will increase the physical capital of a country that leads to an increase in output. Capital accumulation is not only limited to physical capital but also the need for quality of human development capital to manage the available resources (Lubis *et al.*, 2016). The quality of human development has similar or even greater effect in increasing production (Muda, 2017). The improvement on the quality

of human resources will encourage individuals to manage the resources effectively and efficiently. It should be encouraged with adequate infrastructure. The government plays a role in improving infrastructure from local government capital expenditure.

4.2.2. The Effect of Capital Expenditure on Economic Growth

Based on the results of hypothesis test, partially, capital expenditure has no significant effect on economic growth. The probability value of the t-test for capital expenditure variable was 0,0125. Because the probability value was 0,0125 or greater than 5% (0,05), then, it is concluded partially significant.This is in accordance with the research conducted by Nurmainah (2013) and Muda *et al.*, (2017). Capital expenditure has a significant effect on economic growth in East Aceh Regency. It can be seen that the large amount of capital expenditure of the local government can increase the economic growth as seen in the value of gross regional domestic product.

4.2.3. The Effect of Human Development Index on Economic Growth

Based on the results of hypothesis test, it was known that the partial effect of human development index variable statistically significant on economic growth. The probability value of t test for the human development index variable was 0,0268. Because the probability value of the t test is smaller than 5% (0,05) then it is concluded the partial effect is statistically significant.The direct effect of the human development index was known -104676,6 and this value has a negative effect on economic growth which means that any increase in human development index will decrease economic growth. This is in accordance with the research conducted by Pituringsih (2013), which states that the effect of GRDP on HDI is shown negative and significant. The negative effect in this study was due to the value of human development index which fluctuated in the period of 2005-2015 and experienced a very significant decline in 2012 and did not increase significantly in 2012-2015. It was due to the method to calculate the human development index in 2011 had been changed, as the literacy rate and the average length of school were changed to the length of school expectation and the average length of school and still usd the base year of 2005 as a reference, which resulted in a very significant decline in 2012-2015. Thus, the negative effect was also caused by the economic growth which continued to increase while the development index had declined. This result means that an increase or decrease in human development index will change life expectancy, length of school expectation, average length of school and purchasing power parity to be higher or lower. However, the high or low life expectancy, length of school expectation, average length of school and public purchasing power were inversely proportional to economic growth in East Aceh in the period of 2005-2015.

4.2.4. The Effect of Local Government Capital Expenditure, Human Development Index, Economic Growth on Poverty

Based on results of hypothesis test, it was known that the simultaneous effect of the variables of capital expenditure, human development index, and economic growth was statistically significant on poverty. It was known that the simultaneous effect obtained the F-statistic value of 4,363012 and probability value of 0,049601. Since the probability value of the F-test was 0.004552 which is greater than 0,05, it is concluded that the simultaneous effect is statistically significant. The value of coefficient of determination (R2) or R-Square value was 0,828225, means that the variables of capital expenditure, human development index and

economic can explain their effect on poverty for 82,82% and the rest 17,18% are explained by other factors outside this model of estimation. Thus, the second hypothesis proves that capital expenditure, human development index and economic growth have a significant effect on poverty collectively.

4.2.5. The Effect of Capital Expenditure on Poverty

Based on the results of hypothesis test, it was known that the partial effect of the variable of local government capital expenditure was not statistically significant on poverty. The probability value of the t-test for capital expenditure variable was 0,2448. Because the probability value of the t-test was 0,2448 which is greater than 0,05, it is concluded the partial effect is not statistically significant.This is in accordance with the research conducted by Kotambunan, *et al*., (2016) that the effect does not suit the theory. It was because there were still some government programs which were not on target and had not even succeeded in reducing poverty. It was due to the inability of the programs to solve the most fundamental problem occurred in society, so that the results had not been effective. In addition, the existing programs were also considered to be reactive, short-term and partial.

4.2.6. The Effect of Human Development Index on Poverty

Based on the results of hypothesis test, it was known that the partial effect of human development index variable was not statistically significant on poverty. The probability value of the t-test for the human development index variable was 0,4288. Because the probability value of the t-test was 0,4288 which is greater than 0,05, it is concluded the partial effect is not statistically significant.This is not in accordance with research conducted by Kotambunan, *et al*., (2016), because the number of human development index in East Aceh district was too small that had not been effective in reducing poverty.

5. CONCLUSIONS AND SUGGESTIONS

5.1. Conclusions

1. Capital expenditure has a positive and significant effect on economic growth, while the human development index has a negative and significant effect on economic growth.
2. Capital expenditure has a positive and insignificant effect on poverty, while human development index has a negative and insignificant effect on poverty.
3. Capital expenditure and human development index, collectively, have a significant effect on economic growth.
4. Capital expenditure and human development index, collectively, have a significant effect on poverty.
5. Capital expenditure and human development index, collectively, have a significant effect on poverty through economic growth.

5.2. Suggestions

1. In improving the economic growth and reducing the poverty rate, local governments should be wiser in preparing capital expenditure plan in their Regional Budget/APBD. In order to have more effective use of capital expenditure, the amount of the budget can have a direct effect on economic growth and reduce the poverty rate.

2. In addition to improve economic growth, the government must also pay attention to the quality of human capital through education and health to improve the human development index and reduce the poverty rate.

3. The increased economic growth is not certainly able to reduce poverty because economic growth is not spread evenly in every region, so it needs a competitiveness, so that every region can increase its per capita income that will reduce the poverty rate and increase the Human Development Index.

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