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Analysis of the Impact of Budget Deficits on the Economy in Indonesia

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Abstract

A budget deficit is a condition where government expenditure exceeds its income. This can have an impact on various aspects of the economy, both positive and negative. This research aims to analyze the impact of the budget deficit on the economy in Indonesia using the literature study method. Collecting data and information utilizing various sources from reference books, similar previous research results, as well as various journals relating to the problem to be solved. The data analysis technique used is qualitative descriptive analysis. The research results show that a budget deficit can have both positive and negative impacts on the economy in Indonesia. The positive impacts of a budget deficit include: Increasing economic growth, increasing employment opportunities, improving community welfare. However, a budget deficit can also have a negative impact on the economy in Indonesia, including: Increasing inflation, increasing the government debt burden, decreasing the rupiah exchange rate. Based on the research results, it can be concluded that the budget deficit has a complex impact on the economy in Indonesia. The government needs to manage the budget deficit carefully and responsibly in order to maximize the positive impact and minimize the negative impact.

INTRODUCTION

The monetary crisis of the 1990s in Indonesia had a negative impact on the country's economy. When developing countries with impressive economic growth were hit by a storm of crisis, their entire economic structures collapsed, and the collapse of countries such as Yugoslavia and the Balkan countries put their fragile national unity at risk. The ongoing economic crisis and the weak recovery process show how fragile the structure and fundamentals of the Indonesian economy are.

Large-scale monopolies will inevitably weaken society's economic efforts, increase economic inequality, and hinder social progress. The government's borrowing of money from foreign sources exacerbates this problem. National development is getting faster day by day, forcing the government to increase foreign loans, which results in Indonesia suffering from increasingly large debts and budget deficits, as well as decreasing government investment and savings which are insufficient to pay off these foreign debts. (Cindy et al., 2022)

The problem is to keep the deficit within reasonable limits while maintaining compliance, because the country's long-term financial commitments are seriously threatened by the budget deficit. Article 12 paragraph 3 of Law Number 17 of 2003 concerning State Finances regulates that the debt burden must not exceed 60% and the deficit must not exceed 3% of GDP.

Data on the Ministry of Finance's budget deficit from 2015 to 2023 shows that the policy at the time of preparing the APBN was a deficit budget. The deficit is also increasing from year to year. Prior to 2020, the budget was relatively stable. In contrast, the COVID-19 pandemic increased the budget deficit to IDR 947.7 trillion in 2020, halted economic activity in Indonesia, and increased government spending in the health sector to fight the pandemic, requiring social support for the communities most affected. However, in 2021, the budget deficit will decrease to IDR 775.06 trillion, and in 2023 it will reach IDR 486.43 trillion. Indonesia's economic activity is gradually returning to normal and the budget deficit is starting to decline.

In addition, the average budget deficit increased to IDR 313.2 trillion per year between 2015 and 2019, and due to the impact of the COVID-19 pandemic it doubled to IDR 638.48 trillion per year between 2020 and 2024. Real sector development, which is currently the government's priority program to balance infrastructure development, in line with the large government spending. Finally, the government took out large debt loans to meet the infrastructure funding needs. (Pratiwi, 2023)

Indonesia must implement a budget deficit policy to obtain the cash needed to strengthen the economy and increase output, income and overall economic growth. Even though the government has a borrowing plan, this strategy has an impact on the APBN deficit. An increase in interest rates occurs every year on a country's foreign debt, and if payments are delayed, the country's aggregate debt also increases. (Sari & Kuntadi, 2023)

The important impact, whether positive or negative, of a budget deficit on the economy. For example, increasing the amount of money in the economy in any way will cause an increase in the prices of goods and services, which in turn will increase inflation. Compensating for the budget deficit by increasing the money supply also has an impact on increasing the public's demand for money. This is influenced by the decline in the value of money in the economy. In other words, people must increase their spending. (Anwar, 2014)

Therefore, because of its broad impact, research on budget deficits is very interesting. Research related to the budget deficit has been widely discussed in previous studies, including Husriah (2020) which discusses the influence of the state budget deficit on revenue and expenditure on economic growth in Indonesia. These findings indicate that Indonesia's economic growth has been impacted in a significant negative direction by the budget deficit.

Meanwhile, the variables that influence the budget deficit are the subject of research by Sari & Kuntadi (2023) who also examines the relationship between economic growth, foreign debt and world oil prices. These findings show that the rupiah exchange rate and world oil prices have an influence on the budget deficit, but also show that economic growth and foreign debt also have an influence.

These are the reasons for this study, which will examine the impact of the budget deficit on the Indonesian economy.

METHODS

This research uses literature study or library research techniques. Library research is a research activity that involves collecting data and information using various sources from reference books, results of similar previous research, as well as various journals relating to the problem you want to solve. Activities carried out in a structured manner can include collecting, processing and summarizing information using certain methods to find solutions to existing problems (M. Sari & Asmendri, 2020).

The data analysis technique used in this research is a qualitative descriptive method. Qualitative descriptive research is a research method that presents data as it is, without manipulation or other processing. The aim of this research is to provide or clarify a complete picture of events and explain the phenomena that are occurring. It is nothing more than a description of several variables related to the problem under study (Rusandi & Rusli, 2021). This research was conducted with the aim of analyzing the impact of the budget deficit on the economy in Indonesia.

RESULTS AND DISCUSSION

Impact of Budget Deficit on Inflation

Inflation is the general and continuing trend of rising prices. Rising prices of goods and services cause a decrease in people's purchasing power and consumption indirectly through economic growth. This causes a lack of demand and production also decreases. A decrease in real production will ultimately cause a decrease in the country's real GDP, which will affect economic growth. In addition, the government must continue to meet people's needs even though income is decreasing, causing a decrease in income and an increase in the budget deficit. (Satrianto, 2015)

The budget deficit can influence inflation through two channels, namely the first, with the monetary sector which will influence the money supply by printing money, and the second, with the real sector (government spending and income), which then influences aggregate demand. (Maulidina, 2017)

Even though there is a positive correlation between the budget deficit and inflation, this correlation is not significant in the short term. This means that an increase in the budget deficit ratio tends to increase the inflation rate. On the other hand, the budget deficit has a significant long-term impact and is positively correlated with inflation.

Therefore, an increase in the budget deficit of 1% will result in an increase in the inflation rate of 0.76%. This shows that the government's deficit strategy implemented at a certain time will not actually affect inflation this year, but will have an impact in future years or over a long period of time. (Rosyetti & Eriyati, 2011)

Budget deficits, whether financed by money creation or by debt, affect the inflation rate. This deficit affects inflation through the money supply. If the deficit is large, the money supply will also increase, which will result in the inflation rate also increasing. (Kalalo et al., 2016)

Impact of Budget Deficit on Economic Growth

Regression analysis reveals that the budget deficit has a statistically significant impact on economic growth from 1990 to 2022, as indicated by a p value of 0.00 < 0.05 and a regression coefficient of 9.93. This shows that an increase in the budget deficit has a positive and significant impact on economic growth. According to Keynesian theory, increased government spending has the potential to stimulate aggregate demand, leading to a further expansion of the production of goods and services, thereby encouraging economic development. (Rusydi et al., 2023)

Similarly, in research by Akbar (2013), who argues that budget deficits have a beneficial and statistically significant impact on economic growth. If the budget deficit falls by 1 billion, it is estimated that there will be a corresponding increase in economic growth of around 9.93%.

This is different from the results of research (Batubara, 2020) which states that the budget deficit has a negative and significant effect on economic growth, where an increase in the budget deficit will have an impact on slowing economic growth. This is because the allocation of state spending is unproductive.

Then research results (Defarahmi & Zulkifli, 2017) say that the budget deficit does not have a significant impact on economic growth, which means that the debt burden will not have an impact on economic growth in the near future. The allocation of public funds by the government plays an important role in maintaining and encouraging economic development in a country. There are certain state expenditures that have the potential to increase economic development. One of these expenditures is consumer expenditure, where increasing consumption leads to increased economic growth, while decreasing consumption results in decreased economic growth. In addition, increasing capital will encourage economic growth.

Capital expenditures are costs allocated in the budget to purchase assets that generate profits in one accounting period. Capital expenditures include land, equipment, machinery, roads, irrigation and networks, as well as other related asset expenditures. The creation and maintenance of reliable and superior infrastructure in various regions plays an important role in facilitating equitable economic development in all corners of the country, thus leading to equal distribution of community welfare. This also allows capital expenditure related to development procurement to achieve this goal. (Rusydi et al., 2023)

Impact of Budget Deficit on the Exchange Rate

A country's economy is shown significantly by its currency exchange rate. People's attitudes in managing money and the stability of a country's economy will be influenced by exchange rate fluctuations. As a result, Indonesia also experiences exchange rate fluctuations because it uses a floating exchange rate system. The domestic economy will also be affected by the instability of the Rupiah exchange rate. (Ratag et al., 2018)

Indonesia, a country that borrows money from abroad, faces exchange rate fluctuations every year. This problem arises because the loan principal and interest are paid in rupiah at the time of installment payments, while the loan value is determined in foreign currency. The overall payment burden will increase if the value of the rupiah weakens or depreciates against the US dollar. The budget will be exceeded by the amount needed to pay loan interest and principal installments. This means that foreign debt payments have increased significantly. As a result, increasing foreign debt payments will have an impact on increasing the government budget deficit. (Satrianto, 2015)

The rupiah exchange rate affects the APBN deficit. The value of loans whose payments are due increases along with the increase in the value of the US dollar and the decrease in the value of the Indonesian rupiah. This will burden the state budget because debt payments (principal and interest payments) will exceed the previously planned funds distributed for that purpose. The national budget deficit will increase if foreign debt interest rates increase. The actual loan value is expressed in another currency, even though principal and interest payments are paid in Rupiah. (R. Sari & Kuntadi, 2023)

The Impact of the Budget Deficit on World Oil Prices

If world oil prices rise, the government is obliged to allocate large amounts of money to hide the shortage of fuel, so that subsidies will continue to decrease. If the government's savings expectations exceed, the APBN will be in the red zone. And this will immediately cause economic shocks in various fields related to fuel. If oil prices continue to rise, the APBN deficit will also get better.

Changes in the price of Indonesian crude oil on the international market are one of the important factors that influence changes in the APBN based on state revenues and state expenditure, also known as the Indonesian Crude Oil Price. On the state revenue side, the amount of crude oil and electricity subsidies, as well as profit sharing funds, is influenced by changes in oil prices. This is because crude oil procurement costs constitute a large part of the subsidized operator's crude oil production costs.

Because most of PLN's power plants still use crude oil, and the price of crude oil purchased by PT PLN is the price of unsubsidized crude oil, changes in crude oil prices will also affect the amount of electricity subsidy contributions. Therefore, changes in crude oil prices directly impact changes in basic production costs. If the basic electricity tariff does not change, then the electricity subsidy burden, which is the difference between the basic tariff and the basic cost of production, will change along with changes in crude oil prices. Therefore, if crude oil production can be increased, the impact of rising oil prices on the APBN can actually be minimized. The government must continue to monitor oil and gas policies so that they are in line with the targets that have been set so that the APBN is not burdened by fuel imports. When world oil prices soared, there were concerns that this production volume would not be achieved because the APBN was not strong enough to carry the subsidy burden. (Lamkawan, 2020)

There is a positive relationship between the national budget deficit and world oil prices. Rising oil prices on world markets mean that countries will have to pay higher costs to prevent fuel shortages, even if gasoline subsidy allocations continue to be cut or savings exceed projections. This could trigger a state budget deficit. Moreover, this will immediately cause economic shocks in all sectors related to the fuel derivatives industry. The APBN deficit will widen with rising oil prices. (R. Sari & Kuntadi, 2023)

Impact of Budget Deficit on Interest Rates

Interest is a reward given to individuals or business entities for a number of savings or loans, and the interest rate is determined as a percentage. Debt financing through the issuance of Government Securities (SBN), both Government Securities (SUN) and Government Sharia Securities (SBSN), which are guaranteed by the state to pay interest and principal on the securities according to the effective date. The burden of interest payments and SBN issued will increase along with increases in interest rates. If this happens, the budget burden will directly increase and the budget deficit could increase. (Lusiana & Soebagiyo, 2023)

One important indicator of a country's economy is the interest rate. Interest rates as a monetary tool have a big impact on short-term money markets, both domestic and international. Changes in interest rates can affect economic stability in a country. If a country faces a foreign debt repayment crisis, creditors may be able to extend repayment terms, but in return, interest rates will rise. (Qadri et al., 2022).

CONCLUSION

The conclusion is that the impact of the budget deficit on the economy in Indonesia includes, firstly, there is the impact on inflation through the money supply, where the greater the budget deficit, the greater the amount of money in circulation. Second, the impact of the budget deficit on economic growth, where an increase in the budget deficit is associated with a positive and substantial influence on economic growth. Third, there is the impact of the budget deficit on the exchange rate. When the value of the US dollar increases and the value of the rupiah decreases, the value of the loan that will mature also increases. Increasing foreign debt interest rates will increase the national budget deficit. Fourth, the impact of the budget deficit on world oil prices and interest rates.

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