

# CHAPTER I

## INTRODUCTION

### A. Background of Study

Economic growth is how a nation's financial standing keeps improving over time. Economic development can boost employment prospects for people as their income or living standards rise and accelerate population growth. Expanding the variety of employment options in the local area is the primary goal of regional economic development. To do this, local government and individuals must collaborate on regional development initiatives. The provincial government should therefore be able to assess the potential resources required to plan and expand the regional economy with the aid of its residents and using current resources (Arsyad, 2010). One of the major benchmarks that may be used to assess the effectiveness of regional economic development, which is a crucial aspect of national economic development based on the concept of regional autonomy, is economic growth.

The goal of development is to modify social structures, people's attitudes, and state institutions without compromising the basic objectives of economic growth, reduction of income inequality, and expansion of opportunities (Widodo, 2006). Economic growth is prioritized in developing nations like Indonesia because it can support ideologies or objectives that encourage advancements in other facets of society. When the

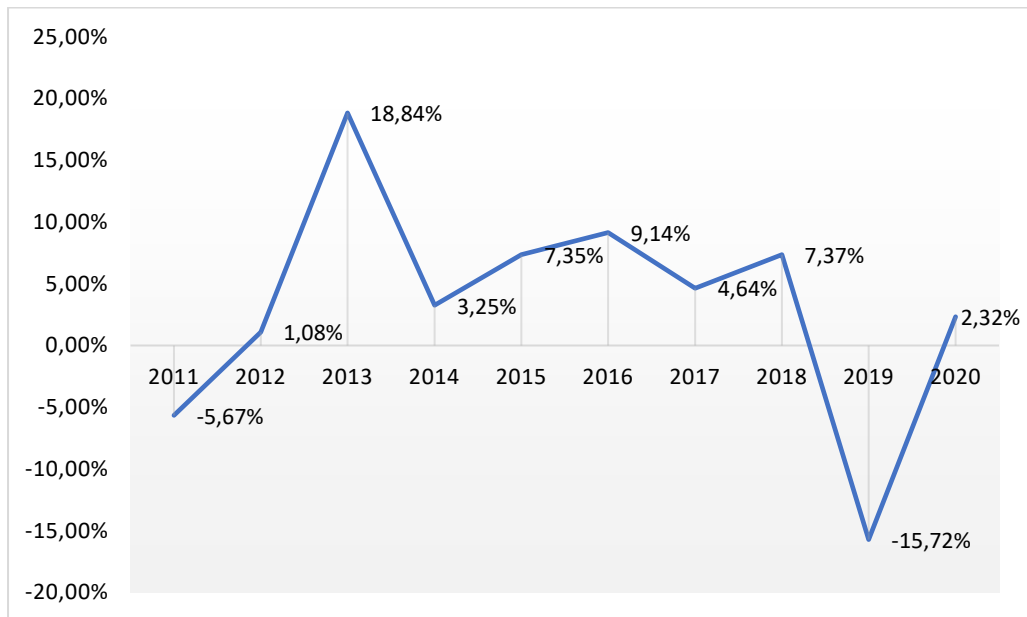
phrase "economic development" is used, it typically conjures images of emerging nations' economy. The phrase "economic development is growth plus change" (as used by certain economists) refers to the expansion of the economy followed by changes to the type and pattern of economic activity (Sukirno, 2011).

Government policies for implementing development, particularly those carried out by autonomous regional governments, constantly seek to enhance, influence, and make and direct changes in the activities of implementing development. The potential resources that a region owns and its capacity to realize that potential have a significant impact on the region's economic health. The potential and natural resources that a region or area owns, as well as its capacity to realize that potential, have a significant impact on the region's economic health. The municipal government has taken a number of policies, actions, and initiatives.

A country's financial status can be continuously improved through monetary development over time. The financial issue of monetary development is a long-term one (Sukirno, 2011). In addition to raising people's prosperity or standard of life, economic development also generates new jobs and may hasten population growth. One of the main goals of regional economic development is to increase the number of employment opportunities for local citizens. To do this, local governments and their residents should work together on local development initiatives. Using available resources and community involvement, local governments must

be able to assess the potential resources required to plan for and develop the local economy (Arsyad, 2010). Money development is one indicator of successful execution of improvements that may be used as a large-scale benchmark. Regional monetary improvement is an important component of the progress of public finance carried out based on regional independence.

On the other hand, various obstacles in maximizing the potential of human and capital resources are still faced by policymakers at the provincial and district/city levels. 2011 Papua Province's economic growth was the lowest, at -5.67%. Subsequently, Papua Province's economic expansion continued in 2012-2013, increasing by 18.84% in 2013 and 1.08% in 2012. However, from 2014 to 2018, economic growth fluctuated between positive and adverse conditions. Due to the impact of COVID-19 in 2019, the economic growth rate of Papua Province decreased by -15.72 percent 2019, causing the Papuan economy also to contract.



**Figure 1** Economic Growth Data of Papua Province 2011-2020

Source: Badan Pusat Statistik (BPS)

Papua Province has also been impacted by the Covid-19 epidemic. To avoid the Covid-19 virus from spreading, the provincial government of Papua has developed a policy that restricts communal activities. The economic success of the area is also impacted by this policy. The economic growth rate in Papua Province stayed same in 2020 at 2.32%. When compared to the Papua Region's monetary development in 2019, which decreased by -15.72 percent this number climbed. The factors driving the acceleration of economic expansion in 2020 are increases in consumption and output.

The main economic growth in Papua Province was driven by an increase in the performance of the mining and quarrying sector, in line with the increase in underground mining productivity. The performance of the

non-mining sector contracted by -6.83% (yoy) during the fourth quarter of 2020, and -3.51% (yoy) throughout 2020. From the expenditure side, household consumption decreased by -7.33% (yoy) in the fourth quarter of 2020 and -5.58% (yoy) throughout 2020. The decline in the non-mining sector was mainly due to the spread of the COVID-19 virus which had a negative impact on economic activity in Papua Province.

According to Malthus in [\(Nanga, 2005\)](#), population growth will quicken if it outpaces economic growth, which is faster than the capacity for economic development. As a result, population growth must be slowed or stopped because any other course will result in joblessness. In [\(Adisasmita, 2013\)](#), Harrod-Domar presents a different perspective in which speculation has a dual economic function, boosting both societal use and monetary development. According to the Neo-Classical viewpoint, technological advancement and the growth in the supply of production-related inputs, rather than consumer demand, drive the rate of economic expansion. The availability of capital and labor as inputs, as well as their productivity, affect the output of goods or services in an economy. In the era of decentralization and regional autonomy, budgetary capacity can be strengthened to satisfy requirements and prevent inequities. Consumption of capital is one strategy for raising revenue.

Economic growth is dependent on macroeconomic factors including government capital spending, investment, and labor. According to [\(Sadono, 1999\)](#) the fiscal economic growth that takes place in a nation is referred to

as economic growth. Examples of this expansion include a rise in the quantity and production of industrial goods, improvements to the infrastructure, an increase in the number of students enrolled in schools, the development of current economic plans, and other developments associated with these elements. Macroeconomic analysis compares the level of the economy to the growth of a nation's real national output, sometimes referred to as GNP or GDP, which stands for Gross National Product.

One form of government spending or expenditure is capital expenditure. Capital expenditures are budget expenditures used in order to acquire or add fixed assets and other assets that provide benefits for more than one accounting period and exceed the minimum fixed asset capitalization limit set by the government. The fixed assets are used not for sale. According to (Nurjoni, 2008), capital expenditure, especially related to infrastructure spending, plays an important role in driving the wheels of economic growth. The development of the infrastructure sector is seen as being able to become the foundation for further economic development. The existence of adequate infrastructure is needed to support higher economic growth, more equitable and more able to prosper the community.

From the APBD of Papua Province in third quarter of 2019, government spending experienced a contraction of -5.21% (yoy). In terms of its components, unexpected spending recorded the highest realization, namely 98,335, while the realization of capital expenditure was still the lowest, amounting to IDR 2.34 trillion or 19.24% of the total capital

expenditure ceiling. the low realization of capital expenditure was due, among others, to delays in the auction process and the appointment of treasury officials. In addition, local government absorption has not been optimal due to the ongoing process of downsizing Papua's regional apparatus organizations (OPD) to 35 OPD after the inauguration of the new governor of Papua.

The next factor that affects economic growth according to the mathematical model is investment. Investments made by the government in order to support the economy are commonly referred to as capital participation. Capital participation if carried out by the central government is called State Capital Participation while if carried out by local governments it is called Regional Capital Participation. Investments made by local governments are expected to increase production factors so that the output produced increases. In addition, the increase in production factors can also have an impact on reducing unemployment.

Investment in Papua in the third quarter of 2019 grew by 14.80% (yoy), an increase compared to growth in the second quarter of 2019 which contracted by -14.48% (yoy). The increase in investment in Papua in the third quarter of 2019 was mainly driven by an increase in gross fixed capital formation (PMTB). PMTB grew by 2.39% (yoy), slowing compared to the previous quarter's growth of 3.02% (yoy). The slowdown in PMTB was generally caused by the low performance of local government spending.

In addition to capital expenditure and investment, labor is also one of the factors that affect the output of a region. A large labor force will be formed from a large population, but population growth is feared to have an adverse effect on economic growth. However, a sufficient number of people with a high level of education and skills will be able to encourage the rate of economic growth. From a large population of productive age, it will be able to increase the number of available labor forces and will ultimately be able to increase output production in a region.

In the August 2019 period the number of people working in Papua increased compared to the February 2019 period, but was accompanied by an increase in the open unemployment rate (TPT) in Papua. The open unemployment rate in Papua in the August 2019 period was 3.65% higher than the February 2019 period of 3.42%. The unemployment rate in Papua is still relatively lower than the national unemployment rate of 5.28%. Until now, not much has changed in the structural transformation of the Papuan economy related to employment, the majority of Papuans work in agriculture, plantations, forestry, hunting and fisheries with a total percentage of 67.73%.

According to (Adi, 2011), Indonesia has a comparatively low employment rate, adding only 250,000 new workers for every one percent of economic growth in the country. Increased investment is anticipated to fuel Papua Province's economic growth. According to Nurkse in Adisasmita (2013), capital formation has the power to end the cycle of poverty in



developing nations. The establishment of offices and foundations that support financial activities, certification of legal certainty, and related regulations and standards that can support and work with ventures are done to produce a more appealing investment environment for financial backers. Government capital spending, investment levels, and labor are anticipated to be the main contributors to Papua Province's increased economic growth as the region's initiator and executor of development.

**Table 1** Potential Natural Resources in Papua Province

Resource Potential	Product
Mineral Resources	Copper, Gold, Silver, Coal, Nickel, Limestone and Clay
Forest Product	Logs, Sawn Timber, Plywood
Plantation Product	Coconut, Coffee, Clove, Nutmeg, Sago, Areca Nut ( <i>Pinang</i> ), Cocoa

Papua Province is one of the provinces in Indonesia which is rich in potential natural resources (SDA). This province has high-value mineral resources, abundant forest products, river resources for large power plants, as well as other potentials such as the extraordinary beauty of natural panoramas. However, this wealth has not been utilized optimally due to the power of several foreign parties and the inability of local residents to manage the assets of the Papua area. Therefore, this study aims to determine the effect of the relationship between the independent variables, namely

capital expenditure, investment, and labor, on the dependent variable, namely economic growth in Papua Province.

The verses related to this research as described in the verse:

لَيْسَ عَلَيْكُمْ جُنَاحٌ أَنْ تَبْتَغُوا فَضْلًا مِّن رَّبِّكُمْ

Artinya: “*There is no sin for you in seeking the bounty of your Rabb.*”  
(*Q.S. Al-Baqarah/2: 198*).

In essence, this study is a replication of Ali Fahmi's research (Fahmi, 2018) which is entitled "Analysis of Determinants of Economic Growth in Jambi Province" using different variables, objects, methods and analysis techniques used. Related to this, researchers are interested in taking the topic for this research is "ANALYSIS OF DETERMINANTS OF ECONOMIC GROWTH IN PAPUA PROVINCE".

## **B. Problem Statement**

Based on the description of the background of the problem above, the problems in this study can be formulated, namely:

1. How does capital expenditure affect economic growth in Papua Province?
2. How does investment affect economic growth in Papua Province?
3. How does labor affect economic growth in Papua Province?

## **C. Purpose of Study**

The purpose of this study is to obtain evidence that:

1. To analyze the effect of capital expenditure on economic growth in Papua Province.
2. To analyze the effect of investment on economic growth in Papua Province.
3. To analyze the effect of labor on economic growth in Papua Province.

#### **D. Benefits of Study**

##### 1. Theoretical Benefits

###### a. For Researchers

Researchers can increase knowledge and insight and implicate and socialize the theory obtained during lectures.

###### b. For Further Research

It is expected to be a reference on capital expenditure, investment, and labor or related to the analysis of the determinants of economic growth in Papua Province.

##### 2. Practical Benefits

###### a. For the Regional Government

Can provide study material for local governments to increase economic growth and can provide information in conducting regional and national economic development policies.

###### b. For the Community

For the community, it can be used as a reference for determining economic growth in Papua Province.