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The Effect of Inflation on Economic Growth in Indonesia in Priode 2015-2023

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ABSTRACT

This research investigates the effect of inflation on Indonesia's economic growth from 1983 to 2014. This research uses descriptive and econometric analysis. This research carries out econometric analysis using simple linear regression (OLS). The research results show that the independent variable has an effect on the dependent variable with a probability value (F-statistic) lower than α = 5%. The t test results show that the inflation variable influences economic growth with a probability value of 74.7588%, while the remaining 25.2412% is influenced by the independent variable.

***Keywords**: Inflation, Economic Growth*

INTRODUCTION

Economic growth is an increase in a country's national income or production from year to year. A country's economic growth can be measured by looking at its gross domestic product (GDP). At present, many countries are trying to encourage their economic growth by continuing to increase production through the availability of capital goods, technology, and human resources. In the context of macroeconomics, inflation is one of the criteria used to observe/measure the stability of a country's economy.

From an economic point of view, inflation is a monetary phenomenon in countries where the ups and downs of inflation tend to cause economic turmoil. Maintaining price stability is still the main objective of macroeconomic policy in most countries around the world to achieve sustainable economic growth. In particular, emphasis is placed on implementing monetary policies that aim to stabilize prices, promote sustainable economic growth and strengthen the purchasing power of the currency. (Umaru and Zubairu, 2012).

Inflation is one of the factors that can affect economic growth. Inflation is the process by which prices generally and continuously rise. Inflation occurs due to several factors that affect the amount of money in circulation: the amount of cash, demand deposits, and quasi-currency circulating in the community (Zulfahmi and Safitriyana, 2012). The more money circulating in society, the lower the exchange rate (purchasing power) and the higher the price of daily necessities.The impact of the coronavirus disease (Covid-19) pandemic has shaken the Indonesian economy, along with the sluggish consumption in Indonesia caused by the spread of the new coronavirus disease (Covid-19). Bank Indonesia Governor Perry Warjiyo said the central bank's concern is that weak consumption leads to a decline in inflation. The inflation rate in May 2020 was recorded very low, at only 0.07% (month-on-month) and 2.19% (year-on-year). "The weak inflation trend seems to continue (Tempo.co in 2020).

However, there are possible disruptions to the global supply chain, and future food price inflation needs to be closely monitored. Nevertheless, domestic product prices remain under control and supply is assured. The central bank expects inflation to remain within its target range this year, at 2-4%. The most significant impact of economic growth is inflation, such as the economic crisis in Indonesia in 1998, where very high inflation paralyzed the Indonesian economy according to (Gregory Mankiw, 2017). From an economic point of view, inflation is a monetary phenomenon in countries where the rise and fall of inflation tends to cause economic turmoil. From an economic point of view, inflation is a monetary phenomenon in countries where the rise and fall of inflation tends to cause economic turmoil. Another impact caused by inflation is that it also affects the operation of financial markets, because it directly affects monetary aggregates in achieving several macro policy objectives such as economic growth, employment opportunities, income distribution, and balance of payments according to (Pohan, 2013). By adjusting the selling price of products in this way, the income they earn is automatically adjusted, often by a larger percentage according to (William A. McEachern, 2013). (William A. McEachern, 2014).

Aggregate demand itself is influenced by prices according to the law of demand: when prices rise, demand falls.According to Keynesian theory, this was achieved by J.M Keynes, Keynes "stated that in the short run national output and employment are mainly determined by aggregate demand".

Researchers are interested in further examining the factors that influence economic growth, namely inflation, because many previous studies have revealed gaps related to these factors. If previous studies used several independent variables, then this study only uses one independent variable, namely inflation. Given that inflation has a relatively large impact on economic growth because it affects both the producer and consumer sides, researchers are only interested in using the independent variable. For consumers, inflation means an increase in the value of a country's currency and the daily purchases of its citizens. On the other hand, inflation can cause economic losses for producers due to increased production costs. In other words, inflation is a factor that has a major impact on the volatility of economic growth. (Mayasari & Mahinshapuri, 2022).

From this explanation, the hypothesis formulation is :

H0 : Inflation does not have a positive and significant effect on economic growth

H1 : Inflation has a positive and significant effect on economic growth

METHODS OF RESEARCH

Independent Variable (X)

The variable that causes the dependent variable to appear and can have a positive or negative impact. In this study, the independent variable is inflation. A situation and condition called inflation occurs when the prices of goods and services continue to increase.

Dependent Variable (Y)

Variables that can be influenced by independent variables. The dependent variable in this study is economic growth in Indonesia. The capacity of a country to grow as a result of the creation of goods and services is generally understood as the definition of economic growth.

Type and Source of Data

This research uses a quantitative methodology and uses secondary time series data ranging from 2015 (quarter I) to 2023 (quarter IV). The documentation technique is used to collect data for this study, which involves finding secondary information from reliable sources to serve as input, especially for analysis and discussion. The secondary data used is sourced from Bank Indonesia and the Central Bureau of Statistics.

Analysis Tool

IBM SPSS 25 for Windows was the tool used to analyze this study. To test the effect of one independent variable on the dependent variable, simple linear regression analysis was used.

Thinking Framework Model

H1: Inflation has a positive and significant effect on Economic Growth

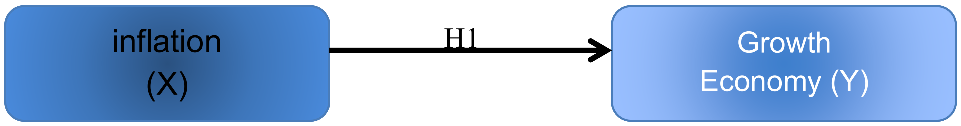


Figure 1. Thinking Framework

RESULTS AND ANALYSIS

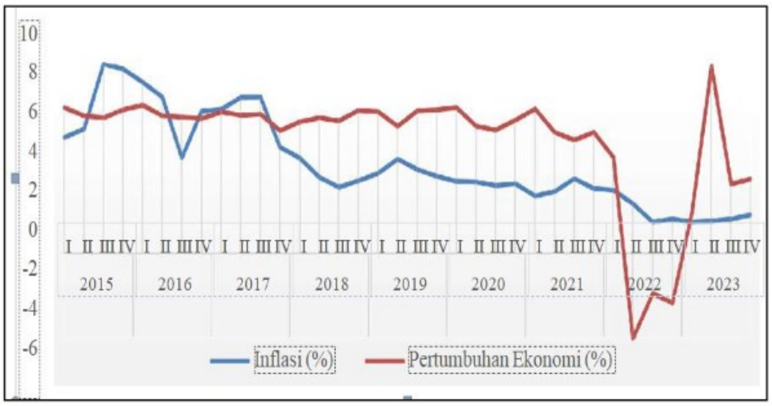
To conduct the simple linear test, researchers used inflation and economic growth data in percent units starting from 2015 (quarter I) - 2023 (quarter IV). It can be seen in table 1 and figure 2, that inflation and economic growth fluctuate from year to year. Here is the data:

Table 1. Table of Inflation and Economic Growth Data in Indonesia per Quarter

Tahun	Triwulan	Inflasi (%)	Pertumbuhan Ekonomi (%)
2015	I	5,26	6,62
	II	5,65	6,25
	III	8,60	6,15
	IV	8,36	6,53
2016	I	7,76	6,72
	II	7,09	6,25
	III	4,35	6,19
	IV	6,47	6,12
2017	I	6,54	6,41
	II	7,07	6,28
	III	7,09	6,32
	IV	4,83	5,58
2018	I	4,34	5,97
	II	3,46	6,15
	III	3,02	6,02
	IV	3,30	6,49
2019	I	3,64	5,97
	II	4,29	6,15
	III	3,81	6,02
	IV	3,50	6,49
2020	I	3,28	6,61
	II	3,25	5,77
	III	3,09	5,61
	IV	3,17	6,05
2021	I	2,62	6,56
	II	2,81	5,5
	III	3,40	5,15
	IV	2,95	5,49
2022	I	2,87	4,37
	II	2,27	-3,84
	III	1,43	-1,8

	IV	1,57	-2,23
2023	I	1,43	1,87
	II	1,48	8,49
	III	1,57	3,15
	IV	1,76	3,38

Data processed, 2023
Source: Bank Indonesia and Central Bureau of Statistics



Tabel 2. Variables Entered/ Renoved

Model	Variabeles Entered	Variables Removed	Method
1.	Inflasi[b]		Enter

a. Dependent Variable: Pertumbuhan Ekonomi
b. All requested variabels entered.

The variables entered and the methods used are described in the table above. In this case, the enter method is used, with inflation as the independent variable and economic growth as the dependent variable.

Tabel 3 Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	,465[a]	,216	,193	2,37807

a. Predictors: (Constant),Inflasi

The correlation or relationship (R) value of 0.465 is explained in the table above. The coefficient of determination (R Square) for this output is 0.216 which indicates 21.6 influence of inflation (X) on growth The regression is:

$$Y = a + bX$$
$$Y = 2{,}720 + 0{,}594X$$

- Which means:

The constant of 2.720 shows the consistency value of the economic growth variable at 2.720. Regression coefficient X of 0.594, economic growth increased by 0.549 for every 1% increase in inflation because the regression coefficient is positive, it can be concluded that variable X has a positive influence on variable Y.

Discussion

It is known that the inflation variable has an influence on the economic growth variable with a significant value of the coefficient table and a significance value of 0.004t Table 2.035 shows that the inflation variable has a positive and significant effect on economic growth. variable These results are in accordance with the theory which states that the increase in production costs due to inflation causes an increase in the price of goods and services so that it has an impact on economic growth. (Ningsih Andiny, 2018) This means that changes in the general price level of a country have a significant impact on economic growth. Research conducted by Moore (2013) is in line with the findings of this study, which found that an increase in the general price level (inflation) affects sustainable economic growth in Tanzania. However, the results of research conducted by Putri et al., (2018) are not in line with the results of this study, it is said that inflation has no significant effect on economic growth, where what gives influence on economic growth is the variable foreign direct investment (FDI) and government spending. This also contradicts Mayasari & Mahinshapuri (2022), The researchers in their introduction stated that inflation is a factor that has a very large impact on economic growth.In the quantity theory which is the most commonly applied theory in relation to inflation.This idea can explain the problem of inflation, especially in developing countries. We can see that in 2020-2021, where the inflation rate was the lowest recorded in history, it was due to covid-19. And this relates to the quantity theory, where the government takes a fiscal deficit budget policy in anticipation of economic growth, which will actually cause the country's debt to increase and, worst case scenario, cause considerable inflation in the future, even though the inflation rate is relatively low (Pratama & Widyastuti, 2022). In terms of monetary policy, inflation has a significant impact on how the general public consumes goods and services and how much money the government invests in gross capital formation. Inflation is a monetary phenomenon that can cause concern for a country (Daniel, 2018).

inflation history

Gold not only had value in a currency, but also had value elsewhere. It is interesting to study the economic history of Byzantium from this perspective. In order to earn gold, the Byzantine Empire tried hard to export as many commodities as possible to other countries and prevented imports from other countries. In the end, people had to buy food, clothing, transportation, and enjoy their lives to spend the money they accumulated. As a result, commodity prices would increase. After the conquistadores era, Spain also experienced the same thing as England after the Napoleonic wars.

The same issue is still debated by economists and financial authorities today, especially since the capitalist era began. Famous names like Adam Smith, David Ricardo, J.M. Keynes, Andrew Jackson, William Jennings Briyan, Charles de Gaulle, Milton Friedman, and Allan Greenspan were involved in the same problem. Inflation hit both the Arab dinar and European currencies such as the UK, France, Spain, Italy, Sweden, Russia, and even the United States. It started even when Iraq was in its prime. Inflation and currency devaluation followed the rapid development of money lending and banking, especially in Italy, which was the catalyst for greater economic growth. Inflation often means slow rather than rapid price increases.

The UK is the only European country that can be considered to have survived inflation successfully, but that was at a time when our economy was seen as poor compared to the rest of Europe. Although highly valued, knowledge of "financial wisdom" has never been the way to achieve prosperity. Due to massive deflation followed by serious social disruption, Britain was forced to discontinue convertibility between sterling and gold, as well as its obsession with high-quality money creation. The return to the gold standard in 1925, which was preceded by several economically destructive policies, was finally halted in 1931. The struggles and hardships were bad enough, but the UK never went back to the gold standard and created superior-quality money.

Inflation Grouping

Inflation Groupings Inflation measured by the CPI in Indonesia is grouped into 7 expenditure groups (based on the Classification of individual consumption by purpose- COICOP), namely:

a. Foodstuff Group
b. Food, Beverage, and Tobacco Group
c. Housing Group
d. Clothing Group
e. Health Group
f. Education and Sports Group
g. Transportation and Communication Group.

The economy is affected by inflation through changes in income and wealth as well as the level and efficiency of production. Creditors, fixed-income groups, and risk-averse investors will be hurt if inflation occurs. (Samuelson, Paul A and Nordhaus, William D, 2014).

Sources of Inflation

The sources that cause inflation are as follows:

a.Demand Pull Inflation

Demand pull inflation is an increase in prices caused by a disturbance (shock) on the demand side of goods and services. An increase in demand for goods that is not balanced by an increase in supply will push prices up resulting in inflation. In demand pull inflation, the increase in the price of final goods (output) precedes the increase in the price of input goods and the price of factors of production (e.g. wage rates).

b.Supply Side Inflation

In contrast to demand pull inflation, cost push inflation is inflation caused by a disruption (shock) from the supply side of goods and services or commonly referred to as supply shock inflation, usually characterized by rising prices accompanied by falling production or output. Thus, inflation is accompanied by a recession. This situation usually starts with a decline in aggregate supply as a result of an increase in production costs.

c.Demand Supply Inflation

An increase in aggregate demand leads to an increase in prices which is then followed by a decrease in aggregate supply, leading to an even higher increase in prices. The interaction between the increase in aggregate demand and the decrease in aggregate supply that pushes up prices is due to the expectation that the price level and wage level will increase or can also be due to the inertia of past inflation.

Types of Inflation

Based on its origin, inflation can be categorized into two types, namely domestic inflation and imported inflation, according to (Nopirin, 2011).

a. Inflation originating from within the country (domestic inflation)

This inflation is caused by a shock from within the country, either due to public action or government action in conducting economic policies.

b. Inflation originating from abroad (imported inflation)

Imported inflation is inflation that occurs in the country due to the influence of price increases from abroad, especially the increase in the price of imported goods also has an impact on the increase in the price of production input goods that still cannot be produced domestically.

CONCLUSIONS AND SUGGESTIONS

This study found the effect of inflation on economic growth in Indonesia. Based on the test results and statistical data analysis, the conclusion of this study is that H1 is accepted, where the inflation variable has a significant value of 0.004 greater than 0.05, this indicates that it significantly affects economic growth. The results of t table and t count have a value of 2.035 and 3.063 respectively. This shows that the inflation variable has a positive effect on economic growth because t count is greater than t table. For the government, there are important policy implications for both domestic policymakers and development partners, which imply that controlling inflation is a necessary condition for promoting economic growth. Thus, policymakers should focus on keeping inflation at a low level. For future research, we can use gross domestic product at constant prices as an indicator of economic growth or other indicators, and for inflation, we can use indicators such as energy crisis, exchange rate volatility, increase in money supply, etc. And we need to test the classical assumptions, to ensure that the data are correct. And it is necessary to test the classical assumptions, to ensure that the regression equation obtained has estimation accuracy, unbiased, and consistent.

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