Journal of Current Studies in SDGs
Homepage : https://journal.i-ros.org/index.php/JOCSIS
Email : jocsis@i-ros.org

e-ISSN 3089-7564
Vol. 1, No.2, June 2025

The Impact of Budget Deficit, Government Spending, and Foreign Debt on Indonesia's Economic Growth

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DOI : https://doi.org/10.63230/jocsis.1.2.30

Sections Info

Article history:
Submitted: April 24, 2025
Final Revised: June 19, 2025
Accepted: June 19, 2025
Published: June 20, 2025

Keywords:
Budget Deficit;
Economic Growth;
Foreign Debt;
Government Expenditure.

ABSTRACT

Objective: *One of the most common things that a country uses as a reference is to know and measure the level of prosperity of its people through the level of economic growth. The purpose of this study is to investigate the impact of budget deficit variables, government spending variables, and foreign debt variables on economic growth. This study focuses on Indonesia as the research location and spans the period from 2000 to 2019.* ***Method:*** *This study employs quantitative calculation methods and multiple linear regression analysis (Ordinary Least Squares), which is processed using EViews software.* ***Results:*** *The study's findings indicate that, partially, the budget deficit and foreign debt have a significant impact on economic growth, while government spending does not have a significant effect on economic growth. While simultaneously, the three variables (budget deficit, government spending, and foreign debt) have a significant effect on economic growth.* ***Novelty:*** *Unlike previous studies, this study utilizes the latest and broader data, focusing on a single country, and finds differences in the results of the influence between variables.*

INTRODUCTION

In a country, a vital measure of the welfare level of its population is the economic growth index (Sukirno, 2015). Economic growth has fluctuated over time. Various indicators can impact economic growth, one of which is the state's role in controlling the economy's circulation. The APBN can support the economic growth process with expenditure variables, debt financing, and deficit policies (Ministry of Finance, 2020). Over the past 24 years (2000-2023), economic development has fluctuated from year to year.

Several factors that influence this are economic variables, including the budget deficit, government spending, and foreign debt. In the first decade (2000-2009), the trend of Indonesia's economic growth showed an average of 5.1%, with the lowest growth point in 2001 at 3.6%, which was caused by domestic political and economic uncertainty in addition to the level of budget deficit at the highest level of 2.8% of GDP and foreign debt owned was 70% of GDP (Ministry of Finance of the Republic of Indonesia, 2001).

Meanwhile, in 2008, many countries worldwide, including Indonesia, faced an economic crisis triggered by the collapse of the central US bank Lehman Brothers, which resulted in a global recession and financial market collapse (Ramadhani, 2014). The crisis could hamper the flow of loan funds between countries (De Haas & Van Horen, 2012). Meanwhile, in the same year, one of the focuses of budget allocation was addressing the Lapindo mud disaster, with an estimated potential economic loss of

16.50 trillion (Bappenas, 2007) as reported by the Kementerian Keuangan Republik Indonesia (2007).

Although the trend is positive, Indonesia experienced an economic downturn at the end of 2020, triggered by the COVID-19 pandemic. Indonesia's economic growth experienced a severe contraction, specifically at a rate of minus 2 (-2). This phenomenon was due to the COVID-19 pandemic, which impacted the safety and health of world citizens, including those in Indonesia. In this condition, the fiscal policy budget deficit swelled by 6.14% of GDP, with a nominal value of 947.7 trillion, which was the most significant percentage in the second decade (2010-2019). Although the nominal value is based on Presidential Regulation Number 72 of 2020 concerning amendments to Presidential Regulation Number 54 of 2020 concerning changes to the posture and details of the 2020 State Budget (Ministry of Finance, 2020), the amount of the budget deficit from 2000-2024 shows a relatively increasing trend (Ministry of Finance of the Republic of Indonesia, 2023).

The same thing is true with the research conducted by Sari & Kuntadi (2023), which implies that spending more on the government's revenue (budget deficit) is a serious long-term problem. Indonesia's debt is not new, but it has been accumulating for a long time. A relatively large amount of debt occurred in 1957 as a result of the nationalization of Dutch companies (Negara et al., 1992). According to Octavianti and Budyanra (2023), the safe limit in measuring foreign debt includes the Debt Service Ratio (DSR), which compares monthly debt installment payments to monthly export income; the safe limit is approximately 40 percent. The application of debt, both domestically and abroad, can cause problems because, in the end, this loan must be repaid, which can drain the country's financial reserves (Lusiana & Soebagiyo, 2023). This study aims to investigate the impact of budget deficit, government spending, and foreign debt on economic growth in Indonesia.

RESEARCH METHOD

Research Population and Data Collection Methods

This research is based on secondary data in the form of time series from 2000 to 2019, with a focus on Indonesia. The data was obtained from the official pages of the Ministry of Finance, Bank Indonesia, and the World Bank.

Analysis Method

The data analysis methodology in this study employs multiple linear regression, which is then processed using the EViews 12 series statistical analysis tool. However, before conducting a multiple linear regression analysis, it is necessary to pass the classical assumption tests, which include a normality test, a multicollinearity test, a heteroscedasticity test, and an autocorrelation test. Mathematically, the multiple linear regression equation of this study can be expressed as Equation 1.

$$\mathbf{Y = a + \beta 1DEF + \beta\ 2PENG + \beta\ 3UTANG + e\ldots} \quad \ldots(1)$$

Description:

Y = Economic Growth

α = Constant

β1 = Budget deficit regression coefficient

β2 = Government expenditure regression coefficient

β3 = Foreign debt regression coefficient

DEF = Budget Deficit

PENG = Government Expenditure

UTANG = Foreign Debt

e = Error Term

Figure 1. Research flowchart

RESULTS AND DISCUSSION

Results

Table 1. Multiple linear regression test results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	7.577921	0.899232	8.427099	0.0000
DEF	-0.625661	0.166251	-3.763346	0.0017
PENG	-0.020346	0.048556	-0.419031	0.6808
UTANG	-0.021177	0.006341	-3.39639	0.0042
R-squared	0.667126		F-Statistic	10.68877
Adjusted R-squared	0.604713		Prob(F-statistic)	0.000422

Based on Table 1, the regression coefficients for the budget deficit variable, government spending, and foreign debt are -0.625, -0.020, and -0.021, respectively. This implies that the regression coefficient is negative. The value of the budget deficit regression coefficient is -0.625, indicating that a 1% increase in the budget deficit level results in a 0.62% decrease in economic growth.

The value of the government expenditure coefficient is -0.020, which means that if the level of government expenditure increases by 1%, it will cause a decrease in economic growth of 0.02%. However, this coefficient is meaningless because, based on the results of the hypothesis test, it does not have a significant effect. The value of the foreign debt regression coefficient is -0.021, indicating that a 1% increase in foreign debt can result in a 0.02% decrease in economic growth.

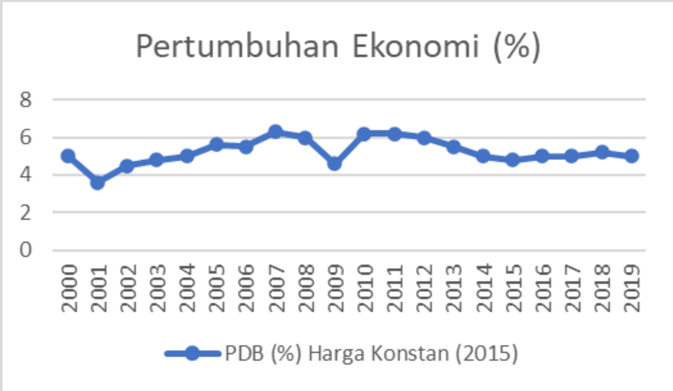

Figure 2. Indonesia's economic growth rate

In the first decade, namely from 2000 to 2009, Indonesia's economic growth trend showed an average of 5.1%, with the lowest growth point in 2001 at 3.6%, which was marked by the existence of domestic political, economic instability, while the high growth rate occurred in 2007 at 6.3% then continued in 2008 at 6% and fell again to 4.6% in 2009 which was partly due to the impact of the global economic crisis in 2008. Furthermore, in the second decade, namely from 2010 to 2019, economic growth increased from 4.6% to 6.2% over the period. Economic growth exhibited a similar trend to that of the first decade, with a rate of around 5.3%.

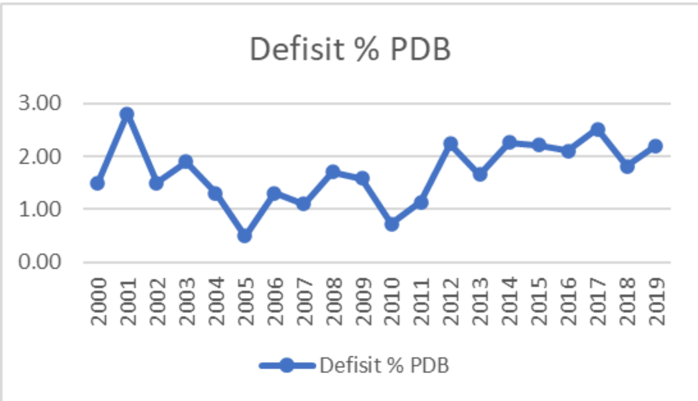

Figure 3. Indonesia budget deficit level

In the first decade (2000-2009), the percentage of the budget deficit fluctuated continuously, with the most significant deficit occurring in 2001, which was 2.8% with a nominal value of 40.5 trillion. Meanwhile, the lowest deficit in the first decade occurred in 2005, which accounted for 0.50% of GDP. This was followed by the second-largest budget deficit in 2008 and 2009, with a percentage of GDP still below 2%, at nominal values of 73.3 trillion and 88.6 trillion, respectively. Meanwhile, from 2010 to 2019, there was a fairly upward trend, but it remained consistent within a 2% deficit range, with an average deficit of 1.88% over the 10 years. The occurrence of a budget deficit is typically related to the management of the state budget, where government spending or expenditure exceeds the government's revenue.

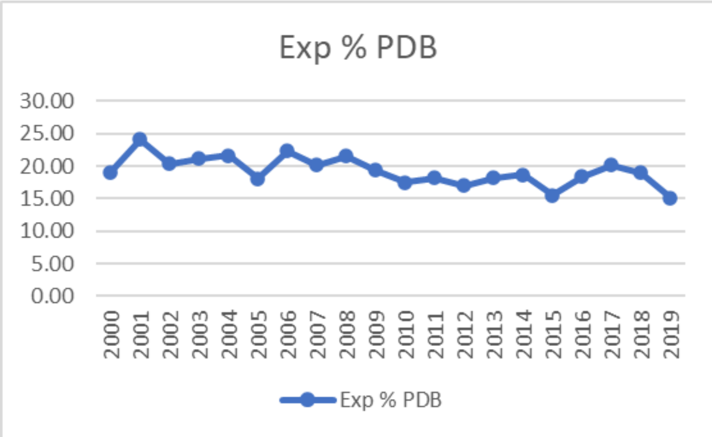

Figure 4. Indonesian government expenditure level

Government spending consistently accounts for around 20% of GDP. Between 2000 and 2009, the highest level of spending occurred in 2001, accounting for 24.10% of GDP. This trend continued into the second decade, specifically from 2010 to 2019, with a decrease in the percentage of GDP. However, in nominal terms, when compared to the previous year, the amount is relatively large, which can be attributed to inflation. Government spending, based on the financial notes of the Ministry of Finance, is divided into two focuses: the first is intended for central spending, and the second for regional transfer spending.

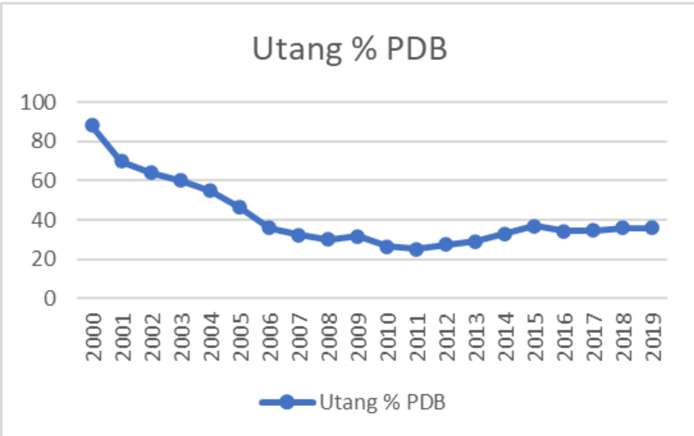

Figure 5. Indonesian government expenditure level

The trend of Indonesia's debt for 20 years (2000-2019) has decreased in percentage, but when viewed in terms of nominal value, the opposite is true. In 2000, the debt-to-GDP ratio was relatively high, at 88.37%, followed by a decrease to 70% in 2001, and then showed a decline throughout the period. The lowest amount of debt was recorded in 2011, at 25.03% of GDP, followed by 2012 and 2013, at 27.41% and 29.13%, respectively. Furthermore, from 2014 to 2019, Indonesia's foreign debt position consistently averaged around 35%.

Discussion

The impact of budget deficit on indonesia's economic growth

Based on the results of the data test in Table 1 above, the budget deficit value has a significant effect on the level of economic growth. The increase in the budget deficit value means that it affects the amount of spending issued by the government, which in turn impacts budgeting costs and economic growth. Additionally, the development of a budget deficit plays a role in accelerating the development carried out by a country. In its implementation, this policy aims to expand economic growth and reduce economic disparities. In Indonesia, the budget deficit is part of the fiscal policy tool outlined in the APBN, which addresses the financing posture, where the financing process is achieved through debt.

The budget deficit has a limit in its application, specifically a maximum of 3% of the gross domestic product (GDP), as stipulated in Law Number 17 of 2003 concerning State Finance (Setjen DPR RI, 2016). Meanwhile, the budget deficit is also very helpful when the country experiences an economic crisis. However, it is often viewed unfavorably by the public because it incurs debts to cover financing. It does not always hurt the economy; it provides a stimulus to the budget that a country's government will spend. The results of this study are supported by Ramadhani's (2014) research, which found that the budget deficit has a significant effect on economic growth.

The impact of government spending on indonesia's economic growth

Based on the results of the data test in Table 1 above, the value of government spending shows no significant effect on the level of economic growth. This event suggests that the quantity of government spending does not necessarily guarantee the same quality, resulting in an economic growth effect that is suboptimal. Since 2000, Indonesia has implemented a budget deficit policy, where the income received by the state is smaller than the expenditure. Therefore, the expenditure disbursed by the state has less influence on Indonesia's economic growth.

Although the impact is less significant, the indicator remains one of the key factors for economic development. Spending disbursed by the government through policies can directly target the main objectives of the target market; in this case, it can be interpreted as the community. The results of this study are supported by the findings of Koyongian and Kindangen (2016), who revealed that government spending has no significant effect on economic growth in the Manado city area.

The impact of foreign debt on indonesia's economic growth

Based on the results of the data test in Table 1 above, the value of foreign debt shows a significant influence on the level of economic growth. The increase in foreign debt also means an increase in economic growth; likewise, when foreign debt decreases, the possibility of economic growth decreases. The results of the regression test conducted show conformity with the Keynesian theory that public debt has been proven to encourage economic growth or have a positive influence on the economy. Foreign debt is part of the financing that serves to cover a country's budget deficit.

The funds obtained will later be used for government programs and investment activities that are expected to attract investors, thereby influencing the level of economic growth. Foreign debt, comprising government debt, Bank Indonesia, and the private sector, can have a significant impact on economic growth because the government and the central bank utilize it to implement policies that have been formulated. The results of the regression test in this study are supported by research from Masri (2021) and Humairah (2023), which state that foreign debt has a significant effect on economic growth.

The impact of budget deficit, government spending, and foreign debt on indonesia's economic growth

Based on the results of the data test in Table 1 above, the value of the budget deficit, government spending, and foreign debt have a significant effect on the level of economic growth. The increase in the three variables also means that it causes an increase in economic growth; likewise, when the three variables decrease, the possibility of economic growth decreases. The budget deficit is implemented to cover financing that cannot be met in the implementation of spending needs on both the central and regional spending sides. All spending aims to run the wheels of the country's economy and must be met with precise calculations; one way to overcome this is by implementing an expansionary fiscal policy.

The budget expenditures carried out aim to run the economy. The results of this study support Wagner's theory, which posits that expenditure increases in proportion to increasing income. However, on the other hand, some factors contribute to high government spending, including the expansion of welfare, security, defense, development, and banking functions (Nahumuri, 2019). Foreign debt is interpreted as similar to loan funds obtained from abroad or creditors (lenders) of foreign organizations who are willing to assist. This foreign debt financing is carried out to accelerate development through the APBN scheme. From this development, it is intended that foreign debt (government debt, Bank Indonesia debt, and private sector debt) can contribute to the effect on capital related to investment, thereby supporting economic growth (Nugraha et al., 2021).

Each indicator that plays an important role in the implementation of fiscal policy occurs as part of a series that cannot be separated. If a country implements a budget deficit policy, the financing typically taken is through debt, both domestic and foreign. Likewise, in the government expenditure indicator, when an expansionary fiscal policy is officially set, the level of spending issued is automatically greater than income. Thus, the greater the level of consumption, the more intense the production activities that occur. The results of the overall regression test are supported by Ramadhani's (2014) research, which found that the budget deficit, government spending, and foreign debt simultaneously influence the level of economic growth, with a focus on the ASEAN region.

CONCLUSION

Fundamental Finding: The study reveals that both the budget deficit and foreign debt have a substantial positive effect on Indonesia's economic growth individually. This means that increases in both variables are associated with higher economic growth. Conversely, when analyzed segmentally, government expenditure does not have a significant impact on economic growth; in fact, increases in government expenditure tend to correlate with a decline in economic growth. However, when analyzed simultaneously, budget deficit, government expenditure, and foreign debt collectively show a significant positive effect on Indonesia's economic growth, indicating that increases across these variables can contribute to higher economic growth overall. **Implication:** The findings underscore the significance of managing fiscal policy, specifically budget deficits and foreign debt, as they are positively correlated with economic growth when effectively managed. Policymakers should carefully assess government expenditure allocation, ensuring that spending effectively contributes to productive sectors that stimulate sustainable growth. The research suggests that a balanced fiscal strategy, which takes into account the complex interactions among these fiscal variables, is crucial for promoting long-term economic development in Indonesia. **Limitation:** This study is limited by its scope, focusing only on budget deficit, government expenditure, and foreign debt. Other influential macroeconomic factors such as inflation, exchange rates, foreign direct investment, and global economic conditions were not incorporated, which may affect the comprehensiveness of the findings. Additionally, the research employs a segmented approach that may not capture the full dynamic interactions over different periods or economic cycles. **Future Research:** Future research is encouraged to expand the model by incorporating additional macroeconomic variables to capture a more comprehensive view of the factors affecting Indonesia's economic growth. Utilizing more diverse and updated datasets could provide deeper insights into the long-term impacts and interactions of fiscal policy instruments within a dynamic global economic environment.

AUTHOR CONTRIBUTIONS

Indah Dwi Agustin*: Conceptualization, Methodology, Investigation, Formal Analysis, Writing – Original Draft, Visualization, Supervision, Validation, Writing – Review & Editing, Project Administration. The author has read and approved the final version of this manuscript.

DECLARATION OF COMPETING INTEREST

The authors declare no known financial conflicts of interest or personal relationships that could have influenced the work reported in this manuscript.

DECLARATION OF ETHICS

The authors declare that the research and writing of this manuscript adhere to ethical standards of research and publication, in accordance with scientific principles, and are free from plagiarism.

DECLARATION OF ASSISTIVE TECHNOLOGIES IN THE WRITING PROCESS

The authors declare that generative artificial intelligence (Gen AI) and other AI-assisted tools were used prudently, not excessively, during the research and preparation of this manuscript. Specifically, ChatGPT was used for brainstorming ideas, structuring paragraphs, and refining academic language; Grammarly for grammar and style correction; and ChatPDF for extracting key points and summarizing reference articles. All AI-generated material was reviewed and edited for accuracy, completeness, and compliance with ethical and scholarly standards. The authors accept full responsibility for the final content of the manuscript.

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