

The Influence of Original Local Government Revenue and Capital Expenditures on Economic Growth and Community Welfare

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Article Info	Abstract
<p><i>Article history:</i> Received September 8, 2023 Revised April 6, 2024 Accepted April 27, 2024 Available online Juni 17, 2024</p>	<p><i>This study examined how capital expenditures and Original Local Government Revenue (PAD) affected community well-being in Bakorwil 1 Madiun, East Java districts and cities between 2015 and 2022. The analysis was mediated by economic growth. This study's saturation sample comprised ten Bakorwil 1 Madiun districts/cities. The Directorate General of Fiscal Balance (DJPK) website of the Ministry of Finance of the Republic of Indonesia provided secondary statistics on the realization of capital expenditures (CE) and PAD. On the Central Statistics Agency (BPS) website, secondary statistics on community welfare (HDI) and economic growth (GRDP) are available for download in different district/city editions for Bakorwil 1 Madiun. Path analysis is used in data analysis. The study's findings indicate that PAD has a significant positive relationship with HDI and GRDP. CE has a significant negative effect on HDI and GRDP partially. GRDP has a considerable positive impact on HDI. GRDP mediates a significant positive effect of PAD on HDI. GRDP does not mediate the impact of CE on HDI.</i></p>
<p>Keywords: Original Local Government Revenue, Capital Expenditure, Economic growth, and Welfare</p> <p>JEL Classification: H71, H75, H76</p>	

INTRODUCTION

Prosperity can only be obtained through planned and sustainable development. The central government intends to accelerate national development through regional autonomy and decentralization. Regional autonomy has made it easier for regional governments to manage their governance by utilizing resources from their regions, which can be used as regional income (Puspitasari et al., 2023). Welfare contains at least three subclassifications, namely: (1) Social welfare, which refers to the collective receipt of welfare; (2) Economic welfare, which refers to guaranteed security through the market or formal economy; and (3) State welfare, which refers to guaranteed social welfare services through agents of the state (Pierson, 2007). Therefore, a welfare state is defined as a nation where the government is charged with implementing development and ensuring every citizen has access to a minimal standard of decent living through sustainable development.

The regional government's implementation of development as a form of decentralization is an effort to achieve its goals (Wijayanti & Darsana, 2015). Decentralization seeks regional independence by facilitating regional growth and development and providing exceptional community service to maximize the region's potential (Haryanto, 2017).

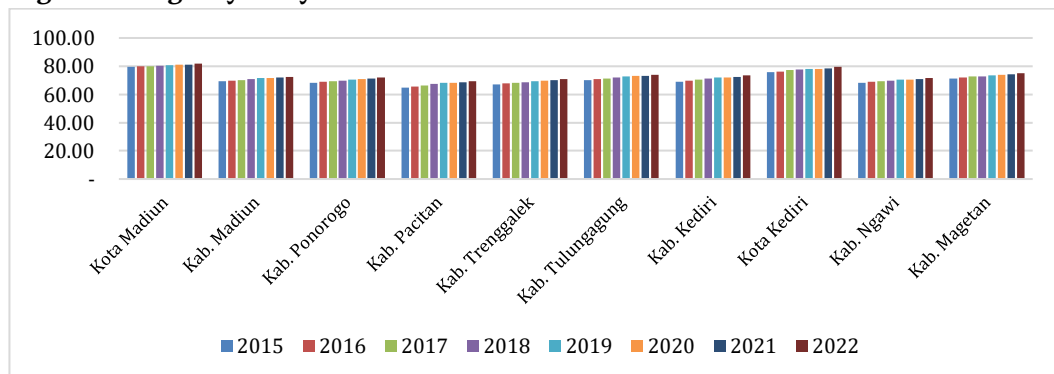
The government uses the Human Development Index (HDI) to assess society's welfare ranking. The field of human development is used as one of the parameters in determining the development of a region (Dianaputra & Aswitari, 2017). Previous research shows that an increase in PAD allows it to increase people's welfare as assessed through HDI (Sari & Supadmi, 2016; Putra & Ulupui, 2015).

The development of community welfare degrees (HDI) for districts/cities in Bakorwil 1 Madiun can be seen (Figure 1) based on the HDI obtained by each district/city in Bakorwil 1 Madiun. Madiun City obtained the best ranking with an average HDI value of 80.63, followed successively by Kediri City (77.65), Magetan Regency (73.16), Tulungagung Regency (72.12), Kediri Regency (71.28), Madiun Regency (71.00), Ponorogo Regency (70.07), Ngawi Regency (70.03), Trenggalek Regency (69.01), and Pacitan Regency (67.37). The welfare state varies from area to region in Bakorwil 1 Madiun. Until recently, government and community policies and interests have made addressing regional disparity their top focus (Irawan, 2015).

One measure of a region's development success is its economic improvement. It can be seen in Figure 2 that the economic growth of districts/cities in Bakorwil 1 Madiun has fluctuated from 2015 - 2022. The disparity in the movement of economic improvement in each district/city is caused by economic activity, resource potential, level of education, and infrastructure. The highest ranking for economic growth in Bakorwil 1 Madiun is Madiun City with an average growth of 4.56%, next in succession are Madiun Regency (4.25), Pacitan Regency (4.00), Ponorogo Regency (3.93), Tulungagung Regency (3.91), Trenggalek Regency (3.90), Magetan Regency (3.89), Kediri Regency (3.81), Ngawi Regency (3.71%) and Kediri City (3.39%). All areas in Bakorwil 1 Madiun experienced the impact of COVID-19, so in 2020, they experienced minus growth. Furthermore, 2021 and 2022 will experience positive economic growth, although slow. As seen in Figure 1 and Figure 2, economic growth does not align with the level of community prosperity (HDI).

Economic growth is not only influenced by regional potential; knowledge and technology can also affect economic growth because they can create innovations that are useful for developing regional potential (Kaur, 2016). One of the main targets for a country's macroeconomic achievement indicators is high and fast economic growth (Maqin & Iwan, 2017). Regencies/cities continue to compete for regional autonomy independence by exploring regional potentials.

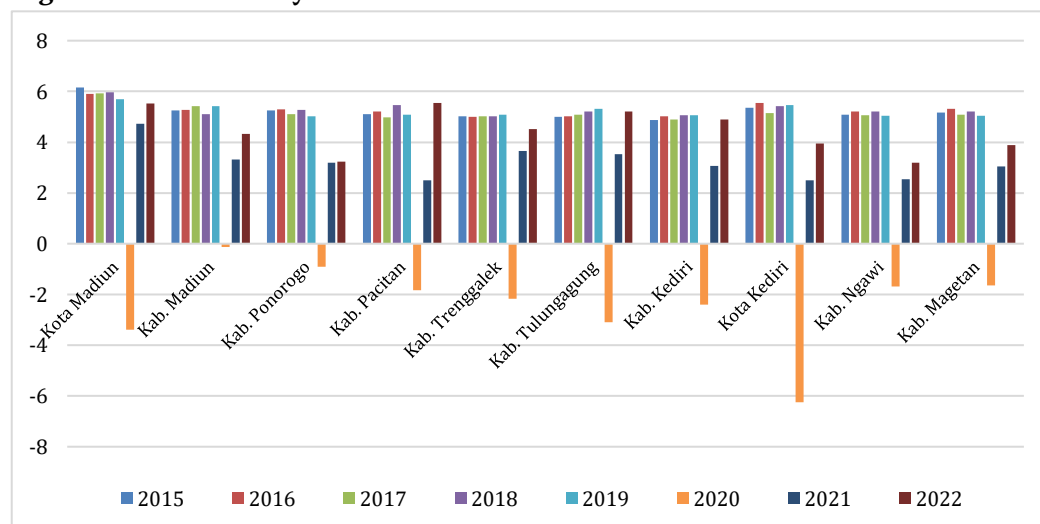
Figure 1. Regency/City HDI in Bakorwil 1 Madiun



Source: Data processed from BPS various editions of Bakorwil 1 Madiun

One measure of a region's development success is its economic improvement. Long-term real income per capita growth is the goal of economic development, which is pursued by institutional system enhancements (Yasa & Arka, 2015). Figure 2 illustrates how the districts and cities in Bakorwil 1 Madiun saw varying economic growth rates between 2015 and 2022. The disparity in the movement of economic improvement in each district/city is caused by economic activity, resource potential, level of education, and infrastructure. The highest ranking for economic growth in Bakorwil 1 Madiun is Madiun City with an average growth of 4.56%, next in succession are Madiun Regency (4.25), Pacitan Regency (4.00), Ponorogo Regency (3.93), Tulungagung Regency (3.91), Trenggalek Regency (3.90), Magetan Regency (3.89), Kediri Regency (3.81), Ngawi Regency (3.71%) and Kediri City (3.39%). All areas in Bakorwil 1 Madiun experienced the impact of COVID-19, so in 2020, they experienced minus growth. Furthermore, 2021 and 2022 will experience positive economic growth, although slow. Economic growth does not correspond with the degree of communal prosperity (as seen in Figures 1 and 2). In order to boost economic activity, reduce regional inequities, and promote national economic development and growth both now and in the future, the government is still putting numerous policies into practice. One of the central policies that are the basis for regional development-based economic development, especially infrastructure transformation, is the prioritization of infrastructure programs/projects, namely through National Strategic Projects (PSN) (Press conference HM.4.6/607/SET.M.EKON.3/10/2022).

Figure 2. District/City Economic Growth in Bakorwil 1 Madiun



Source: Data processed from BPS various editions of Bakorwil 1 Madiun

To realize regional autonomy and fiscal decentralization, regional governments need to compete to explore their PAD potential. "PAD is income obtained by the region which is collected based on regional regulations by statutory regulations" (Law Number 33 of 2004).

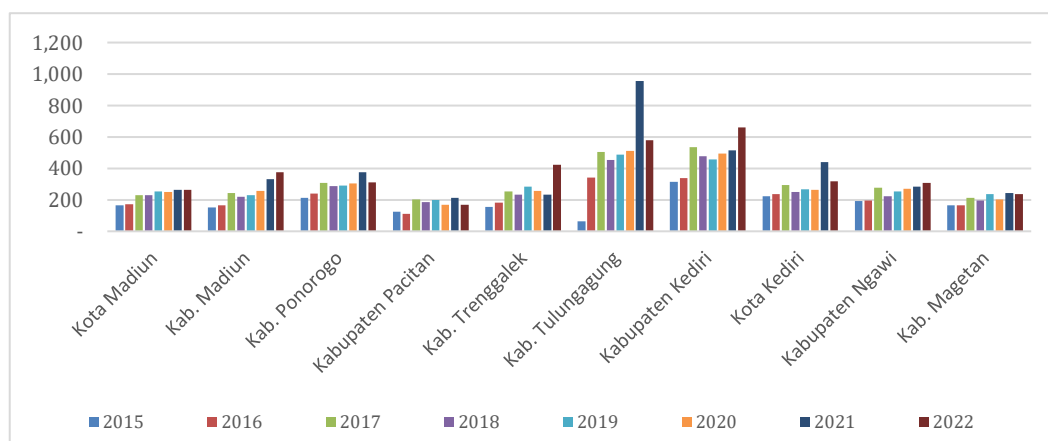
The PAD can be a standard for gauging a region's financial autonomy for regional development initiatives. Of course, improved public services will increase societal prosperity, and the HDI will rise (Putra & Ulupui, 2015).

Figure 3 shows the figures for realizing PAD for 2015 - 2022 in districts/cities at Bakorwil 1 Madiun. For eight years, PAD experienced fluctuations, with Tulungagung Regency obtaining the first rank, followed in succession by Kediri Regency, Ponorogo Regency, Kediri City, Trenggalek Regency, Ngawi Regency, Madiun Regency, Madiun City, Magetan Regency, and Pacitan Regency.

Various studies on PAD conclude that PAD significantly impacts economic growth (Yunus & Amirullah, 2019; Utami & Indrajaya, 2019; Monica & Sa'roni, 2022). Other research shows the opposite; PAD does not significantly affect economic growth (Wau & Mendrofa, 2022). PAD significantly affects HDI (Verawaty & Salwa, 2023).

Capital expenditures for public services will be more productive than those used for regional apparatus (Triyanto et al., 2017). Previous research shows that capital expenditures significantly impact economic growth (Putra, 2016; Fitrah et al., 2021; Utami & Indrajaya, 2019).

Figure 3. Realization of Regency/City PAD in Bakorwil 1 Madiun



Source: Data processed from APBD Posture

Capital expenditures include direct government expenditures related to government activities. They are categorized as public and apparatus spending (Kepmendagri Number 29/2002). Capital expenditures aim to enhance public services in health, education, the economy, etc.

Regional governments' task to increase economic growth is effectively allocating government spending to support economic activities such as building public infrastructure. By appropriately allocating government spending, regional income is hoped to increase (Kusuma, 2016). Economic growth positively affects community welfare (Utami & Indrajaya, 2019; Wijayanti & Darsana, 2015; Rosita & Sutrisna, 2018).

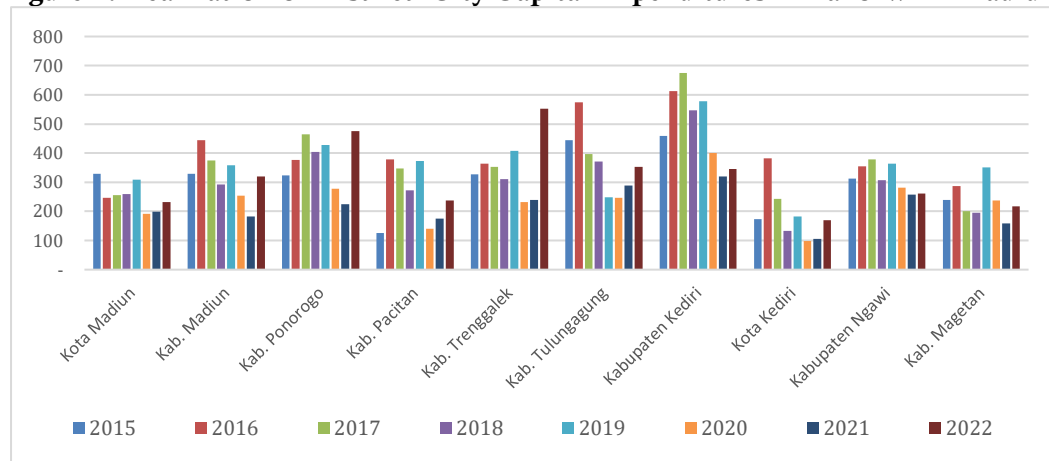
Economic growth is a mediating variable for the effect of regional original income on people's welfare. However, economic growth is not a mediating variable for the effect of capital expenditure on people's welfare (Utami & Indrajaya, 2019). Figure 4 shows data on the realisation of capital expenditure in districts/cities in Bakorwil 1 Madiun for 2015 – 2022.

John Maynard Keynes (1936) conveyed the thoughts of the Keynesian Revolution macroeconomic theory. Keynesian theory is directed towards effective aggregate demand in the country for strategic variables to solve the stagnation of production aspects. Consumption, investment, and government spending all benefit economic activity and lower unemployment when there is effective aggregate demand in the nation. Keynes's theory was driven by the 1929–1930 Great Depression, which made it appropriate for stabilizing the short-term rather than addressing long-term developmental issues (Arif, 1998, p. 28).

The Keynesian theory states that increasing government spending/spending will increase planned spending, income, and economic growth (Mankiw, 2007, p. 277). Keynes' theory states that government spending influences economic growth (Azwar, 2016). In line with Keynes's theory, Harrod Domar's theory suggests that in order to achieve a stable economic situation, capital formation is necessary in the country concerned.

According to WW. According to Ansofino et al. (2020: 12), there are five stages of modern economic growth: "traditional society, pre-takeoff, take-off, movement towards maturity, and high consumption."

Figure 4. Realization of District/City Capital Expenditures in Bakorwil 1 Madiun



Source: Data processed from APBD Posture

From 2015 to 2022, the most significant capital expenditure realization was Kediri Regency, followed by Ponorogo, Tulungagung, Trenggalek, Madiun Regency, Ngawi, Pacitan, Madiun City, Magetan, and Kediri City. In every district and city across Bakorwil 1 Madiun, the community's welfare can be improved by raising capital expenditure and PAD in conjunction with precise target allocation.

Increased PAD and capital expenditure are expected to encourage economic growth and welfare. This is provided that decisions on the allocation of PAD and capital expenditure are based on development needs and priorities. Increased per capita income, income equality, job creation, and improved welfare can be influenced by economic growth. Economic growth is crucial to achieving regional welfare. Thus, one measure of the effectiveness of regional autonomy is the degree of welfare. The researchers wish to examine the degree to which economic factors mediate the

influence of capital expenditure and PAD on welfare cohesion in Bakorwil 1 Madiun, East Java, based on the evidence that has been given.

This study aims to investigate the following topics: 1) The impact of PAD on welfare; 2) The impact of capital expenditures on welfare; 3) The impact of PAD on economic growth; 4) The impact of capital expenditures on economic growth; 5) The impact of economic expansion on community well-being; 6) The indirect relationship between PAD and community welfare, which is mediated by the region's economic expansion; and 7) The relationship between capital expenditure and community well-being, which is mediated by the region's economic expansion.

RESEARCH METHODS

This study uses an explanatory and quantitative method. A population is a broad category of items or persons with specific attributes chosen by researchers for analysis before conclusions are drawn (Sugiyono, 2015). The regency/cities of Madiun 1 Bakorwil, specifically Madiun, Ponorogo, Pacitan, Trenggalek, Tulungagung, Kediri, Ngawi, and Magetan, comprise the saturated sample for this study. Next, Kediri City and Madiun City

The realization (posture) of the APBD from the website of the Directorate General of Financial Balance (DJPB), Ministry of Finance of the Republic of Indonesia, and secondary data from the BPS website of various editions of Bakorwil 1 Madiun are used in this study. Total $n = 8 \text{ years} \times 10 \text{ districts/cities} = 80$ is the observation year 2015–2022.

Hypothesis Formulation

The following framework, prior research, theoretical studies, and background information are the basis for developing hypotheses.

H1: PAD has a significant positive effect on community welfare

H2: Capital expenditures influence community welfare

H3: PAD has a significant positive effect on economic growth.

H4: Capital expenditure has a significant positive effect on economic growth.

H5: Economic growth has a significant positive effect on welfare.

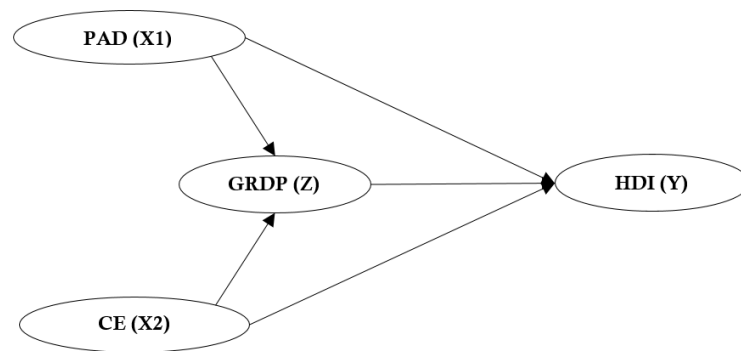
H6: PAD has a significant positive indirect effect on welfare through economic growth.

H7: Capital expenditure has an indirect effect on welfare through economic growth.

Framework

The framework of thought is arranged based on the logic of the relationship between variables. The independent variables of this research are PAD and Capital Expenditures (CE). The mediating variable is Economic Growth with constant price GRDP proxies. The dependent variable is welfare through a proxy for the HDI. Figure 5 explains the partial direct effects of PAD, CE, and GRDP on HDI. How partially the direct effect of PAD and CE on GRDP. Furthermore, it shows how the indirect effect of GRDP can partially mediate the effect of PAD and CE on HDI.

Figure 5. Framework of Thought



PAD: Original Local Government Revenue; CE: Capital Expenditures; GRDP: Gross Regional Domestic Product (Economic Growth); HDI: Human Development Index (Community Welfare)

Variable Operational Definitions

"PAD is all regional revenue originating from original regional economic sources, consisting of regional taxes, regional levies, proceeds from regionally owned companies and the results of management of separated regionally owned assets, other legitimate PAD" (Halim, 2007).

"Capital expenditure is realized in the form of procurement of fixed assets or other assets that support the implementation of regional government activities, have a useful life of more than twelve months, and meet the minimum threshold for asset capitalization value" (Permendagri Number 77/2020).

"Economic growth shows more quantitative changes and is usually measured using Gross Regional Domestic Product (GRDP) or income or final market value of final goods and services produced in an economy during a certain period" (Etika et al., 2022).

"The Human Development Index (HDI) is a concept from the UNDP program to tackle poverty with priorities, namely three index standards arranged systematically, namely education, health, and purchasing power" (Hariwan & Swaningrum, 2015). The HDI is a tool used to evaluate a region's degree of development success. The HDI classification, according to the Central Bureau of Statistics, is very high (HDI > 80), high (HDI 70-80), moderate (HDI 60-70), and low (HDI < 60).

Statistical Testing

Path analysis via the SmartPLS 3 program is used in data analysis, where the research variables are Natural logarithm (Ln) PAD, Ln Capital Expenditures, and Ln GRDP. "Testing statistical data is the Q Square test to measure how well the model generates the observed values and parameter estimates" (Ghozali, 2016). A predictive relevance number for the model is shown by a Q-Square value greater than zero. "If the Q-Square value is less than 0 (zero), then the model has less or no predictive relevance" (Chin, 1998). "The predictive relevance figure is obtained by the formula: $Q^2 = 1 - (1 - R1^2) (1 - R2^2) \dots (1 - Rn^2)$ " (Hair, 2011). Additionally, the hypothesis was tested using direct and indirect (mediation) methods. If the significance level is \leq

0.05, variable X influences Y and has a noteworthy impact when T Statistics is more significant than T Table.

RESULT AND DISCUSSION

Q Square Testing

$$Q^2 = 1 - (1 - R1^2)(1 - R2^2)$$

$$Q^2 = 1 - (1 - 0.258)(1 - 0.419)$$

$$Q^2 = 0.569$$

With a Q-Square of 0.569 or 56.9%, the research model has a valuable prediction value and can account for 56.9% of the research data.

Analysis of Direct Effects

H1: PAD considerably enhances community welfare (HDI) in districts/cities in Bakorwil 1 Madiun, with a significant figure of $0.003 < 0.05$ and T statistics 3.031 ($> T$ Table 1.990). Thus, hypothesis 1 is agreed upon. Community welfare will increase by 0.210 for every unit added to PAD, based on the interpretation of the coefficient value 0.210.

Hypothesis 2 is approved since Capital Expenditure (CE) significantly reduces welfare in districts and cities throughout Bakorwil 1 Madiun (significant number $0.000 < 0.05$ and T Statistics 3.698 ($> T$ Table 1.990)). If capital expenditures are increased by one unit, community welfare will have an impact of -0.368, according to the interpretation of the coefficient value of -0.368.

Table 1. Analysis of Direct Effect

H	Connection	Coefficient	t Statistics	Significance	Conclusion
H1	PAD → HDI	0.210	3.031	0.003	Significance
H2	CE → HDI	-0.368	3.698	0.000	Significance
H3	PAD → GRDP	0.472	4.735	0.000	Significance
H4	CE → GRDP	-0.291	2.031	0.043	Significance
H5	GRDP → HDI	0.379	2.641	0.009	Significance

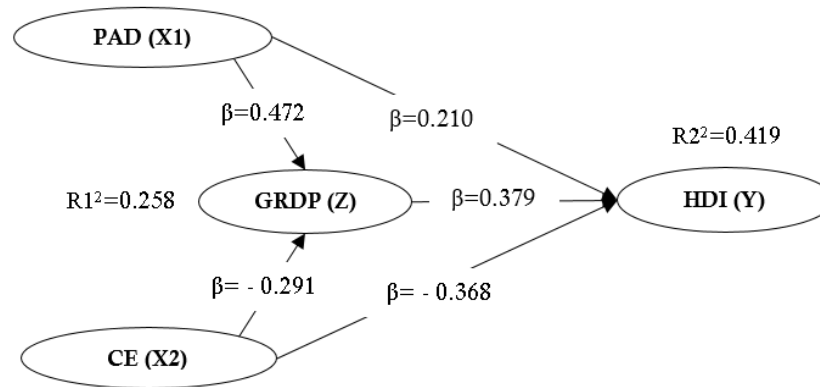
H3 confirms hypothesis 4: With a significant number of $0.000 < 0.05$ and a T statistic of 4.735 ($> T$ Table 1.990), PAD has a substantial effect on economic growth (GRDP) for districts/cities in Bakorwil 1 Madiun. According to the interpretation of the coefficient value of 0.472, economic growth will increase by 0.472 for every point increase in PAD.

H4: With a significant figure of $0.043 < 0.05$ and T Statistics 2.031 ($> T$ Table 1.990), Capital Expenditure (CE) has a substantial adverse effect on economic growth (GRDP) for districts/cities in Bakorwil 1 Madiun, indicating that hypothesis 5 is accepted. If capital expenditures rise by one unit, the coefficient of -0.291 can be understood to indicate that economic growth has a negative impact of -0.291.

Hypothesis 3 is supported because H5: Economic growth (GRDP) significantly improves community welfare (HDI) in districts and cities throughout Bakorwil 1 Madiun, with a significant number of $0.009 < 0.05$ and T Statistics 2.641 ($> T$ Table 1.990). One way to interpret a coefficient of 0.379 is to say that society's welfare will also increase by 0.379 for every unit rise in economic growth.

Figure 6 illustrates each exogenous variable's potential to influence the exogenous variable, leading to the conclusion that PAD significantly improves HDI. HDI is significantly impacted negatively by CE. PAD significantly impacts GRDP. GRDP is significantly impacted negatively by CE. Lastly, HDI is very positively impacted by GRDP.

Figure 6. Parameter Estimates for the Final Model



Analysis of Indirect Effects

Because the significant value is $0.014 < 0.05$ and the T statistics are $2.463 (>T$ Table 1.990), PAD has a significant positive indirect influence on community welfare (HDI) through economic growth (GRDP). Thus, the hypothesis is supported. Consequently, hypothesis 6 is approved. According to the coefficient of 0.179 , welfare has an indirect positive effect mediated by economic growth of 0.179 for every unit increase in PAD.

Table 2. Analysis of Indirect Effects

H	Connection	Co.	t Statistics	Sig.	Conclusion
H6	PAD → GRDP → HDI	0.179	2.463	0.014	Significance
H7	CE → GRDP → HDI	-0.110	1.518	0.130	No Sig.

H7: Economic growth (PE) mediates community welfare (KM), and capital expenditure (CE) does not have an indirect negative influence on KM. Therefore, hypothesis 7 is rejected because the T statistic is $1.518 (< T$ Table 1.990), and the significant value is $0.130 > 0.05$. It is possible to deduce from the coefficient value of -0.110 that if capital expenditures rise by one unit,

The Effect of PAD on Community Welfare

The present study concludes that PAD significantly and favorably affects community welfare in districts and cities across Bakorwil 1 Madiun. This finding aligns with the studies conducted by [Sari and Supadmi \(2016\)](#). [Putra and Ulupui \(2015\)](#) and [Verawaty and Salwa \(2023\)](#) concluded that people's welfare may rise with a rise in PAD (HDI). Regional original income, or PAD, is a source of funding for regional governments to implement development initiatives that lead to prosperity. As a means of decentralization, PAD aims to incentivize the regional government to adjust the region's autonomy by its potential to increase prosperity (HDI).

Effect of Capital Expenditures on Community Welfare

According to the results of the current study, capital expenditures in regencies/cities such as Bakorwil 1 Madiun significantly worsen welfare. Infrastructure must incur capital costs to deliver public services, with the ultimate aim of enhancing the welfare of the populace. Capital investments for community welfare initiatives must be a greater priority for local governments. Capital expenditure that is right on target and efficient will improve people's welfare, such as improving educational facilities. Health and unemployment reduction. This research supports previous research but goes the opposite, concluding that capital expenditure significantly impacts economic growth (Putra, 2016; Fitrah et al.; [Utami & Indrajaya, 2019](#)).

Influence of PAD on Economic Growth

According to recent research, PAD significantly boosts economic growth in districts and cities in Bakorwil 1 Madiun. Current research fits with the Keynesian Theory, which explains, "an increase in government spending/spending will increase planned spending. It will increase income and economic growth" ([Mankiw, 2007: 277](#)). It can be interpreted if PAD rises. Then, spending will also increase, causing an increase in economic growth if PAD grows. Then, the degree of fiscal dependence of a region on the central government will decrease. Regional governments with high PAD will be more flexible and more accessible in preparing and spending their budgets according to needs. The present investigation validates the findings of other studies that PAD has a positive and significant effect on economic growth ([Yunus and Amirullah, 2019](#); [Utami and Indrajaya, 2019](#); [Monica & Sa'roni, 2022](#)). But contrary to research. PAD does not significantly affect economic growth ([Wau & Mendrofa, 2022](#)).

Effect of Capital Expenditures on Economic Growth

According to recent investigations. Capital expenditure significantly impacts economic growth in districts and cities in Bakorwil 1 Madiun. This is achievable since industries that promote economic growth have not received the majority of capital expenditures. However, other areas, like health, education, and other infrastructure, continue to receive precedence. It should be if capital expenditure increases. It can encourage economic development. Capital expenditure is direct spending in the government budget with fixed output assets, especially for public services. Capital expenditures can stimulate regional economic growth, and people must be encouraged to distribute their income. The results of this study validate the findings of earlier studies. Capital expenditures significantly impact economic growth ([Putra, 2016](#); [Fitrah et al., 2021](#); [Utami and Indrajaya, 2019](#)).

How Economic Growth Affects Welfare

The current study's results indicate that economic expansion significantly improves people's welfare, which aligns with earlier research. Economic progress benefits community well-being ([Utami & Indrajaya, 2019](#); [Wijayanti & Darsana, 2015](#); [Rosita & Sutrisna, 2018](#)). Regional governments must support and promote economic

growth because rising HDI will affect people's well-being in districts and cities like Bakorwil 1 Madiun.

How Capital Expenditures and PAD Affect Community Welfare through Economic Growth

Research results now. Economic growth mediates PAD on welfare in a positive direction. One way to measure a region's progress is through its economic growth. Community prosperity and PAD will rise as a result of economic growth factors. PAD continues to increase good economic growth. Controlled inflation needs to be encouraged in order to create social welfare. However, economic growth does not mediate capital expenditure on public welfare in a negative direction. The reason is that capital expenditure is still spent on public infrastructure and has little direct contact with economic growth and community welfare. The COVID-19 pandemic that struck in 2020 and 2021 caused the government to allocate additional funds to managing the pandemic's effects. Furthermore, the early years after the pandemic were still in the economic recovery phase. The Keynesian-Domar hypothesis holds that capital investment is necessary to promote economic growth. Therefore, the Regional Government must allocate capital expenditures in an effective, efficient manner, taking into account the post-pandemic priority scale.

The current study backs up earlier studies. Growth in the economy moderates the impact of PAD on social welfare, but it does not mitigate the impact of capital expenditure on social welfare (Utami and Indrajaya. 2019). Economic growth is a critical factor in increasing people's welfare. Economic growth can be achieved if PAD increases. So, based on Rostow's theory of economic growth. Local government needs to reach economic maturity, where the economy needs to be directed to regular growth. Creation of business opportunities. Massive application of modern technology followed by an increase in investment and savings.

CONCLUSION

It significantly improves community welfare and economic progress in terms of PAD. This indicates that PAD can promote more economic growth and welfare in the neighborhood. The improvement of the economy and welfare are significantly harmed by capital expenditure. Infrastructure procurement continues to receive capital expenditure priority even though this has no direct impact on welfare or economic growth. Welfare benefits greatly from economic expansion. The positive relationship between PAD and welfare is mediated by economic expansion. Economic progress will encourage the development of social welfare. The adverse impact of capital expenditure on the well-being of individuals is not mitigated by economic growth.

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