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THE EFFECT OF REGIONAL FINANCIAL PERFORMANCE ON CAPITAL EXPENDITURE AND ECONOMIC GROWTH IN EACH DISTRICT / CITIES IN BALI PROVINCE

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Abstract

Regional financial management aims to fulfill the principles of value for money both in terms of income and expenditure economically, effectively and efficiently. The purpose of this paper is to determine the effect of regional financial performance on capital expenditure significantly, to determine the effect of capital expenditure on economic growth significantly, and to determine the indirect effect of regional financial performance on economic growth. This study uses census data which are all districts and cities in the province of Bali. The analysis technique used is SEM (Structural Equation Model) with the help of PLS program. The data used in this study is time series from 2012-2016. The results of the analysis found that the relationship between financial performance on capital expenditure had a significant effect, capital expenditure on economic growth had no significant effect, and the regional financial performance on economic growth had no significant effect.

Keywords: Regional Financial Performance, Capital Expenditures, Economic Growth, Significant, Regional Financial Ratios

INTRODUCTION

Equitable development in all regions in Indonesia is a goal of the government which is stated in Law No. 22 of 1999 concerning Regional Autonomy. Subsequent developments were an improvement of the 2001 regional autonomy policy which underwent enormous changes in regional financial management. Regional financial management arrangements are further refined by Undang-undang (state law of Indonesia) No. 32 of 2004 and No. 33 of 2004 which will later be used as the main foundation in the management of regional autonomy, where this law is about regional governance that focuses on the autonomy authority given to each district / city. The implementation of regional autonomy is supported by Undang-undang No. 32 of 2004 concerning Regional Government and Undang-undang No. 33 of 2004 concerning Financial Balance between the Central and Regional Governments.

The existence of good financial management is expected to affect regional progress both economically, effectively and efficiently, so that it is expected to encourage economic growth (Sularso and Restianto, 2011). As research conducted by Mbedzi and Gondo (2010) results in inefficiencies in financial performance against capital expenditure. Adi (2006) mentions that there are three basic components in measuring economic growth including: capital accumulation, population growth, and things related to the increase in the number of labor force that are considered to positively stimulate economic growth. By that components, capital accumulation is a component that can be investigated and seen in quantitative developments that are related to regional finances (Sulaso and Restianto, 2011). Capital expenditure allocation is related to the development of an area's performance as expressed by Ardhini and Handayani (2011) where financial performance as measured by its ratios has a significant influence on capital expenditure. But Expenditures from excessive capital expenditures can reduce economic growth and performance such as research produced by Devarajan et al. (1997). Where research is conducted in developing countries, if spending is used productively, it will have a positive influence on economic growth, but if used excessively, this expenditure is no longer productive, resulting in a decline in economic growth.

Based on the description of the background, the main problems in this research are: What is the influence of the Regional Financial Performance on Capital Expenditures? What is the influence of Capital Expenditures on Economic Growth? What is the effect of Regional Financial Performance on Economic Growth?

RESEARCH PURPOSE AND SIGNIFICANCE

Based on the problem that proposed in this research, the research objectives are as follows: to determine the effect of regional financial performance on capital expenditure, to determine the effect of capital expenditure on economic growth, and to determine the effect of regional financial performance on economic growth.

The theoretical benefits of this research are: this research is expected to contribute to science, technology and art, especially donations for academics in examining policy implementation regarding regional financial performance, capital expenditure, and economic growth and the results of this study are expected to be a supporter as well as a reference in future research.

Practical benefits in this study are: as information to the public and management of District and City Governments in Bali Province concerning Regional Financial Performance, Capital Expenditures, and Economic Growth, as information to the Government and the Government regarding the influence of financial performance on the allocation of capital expenditure and economic growth as well as guidelines for other researchers for further research on regional financial performance, capital expenditure and economic growth.

LITERATURE REVIEW

Government Financial Performance

Local government financial performance can be measured by assessing the efficiency of the realization of the allocation made by the government on a budget. Regulation of the Minister of Home Affairs (Permendagri) No. 13 of 2006 states the definition of performance as follows, performance is the output / results of activities / programs that will or have been achieved in connection with the use of the budget with measurable quantity and quality. Performance measurement has several objectives. In general, the purpose of performance measurement (Mardiasmo, 2005: 122) is: for better communicating strategies, to measure financial and non-financial performance in a balanced manner so that the development of achievement strategies can be traced, to accommodate understanding of the interests of middle and lower level managers and motivate to achieve suitability of objectives, and as a tool to achieve satisfaction based on individual approaches and rational collective capabilities.

A performance indicator is a variable used to express quantitatively the effectiveness and efficiency of a process or operation by referring to organizational goals and objectives. To understand financial ratios as a company performance analysis instrument that describes various relationships and financial indicators that are intended to show changes in financial conditions or past operating achievements and help illustrate the trend of these change patterns to show the risks and opportunities inherent in the company concerned. This shows that financial ratio analysis is based on past data and conditions but is intended to assess risks and opportunities in the future. Halim (2008: 45) states that financial performance analysis is an attempt to identify financial characteristics based on available financial statements. In government organizations to measure financial performance there are several measures of performance, namely independence ratios, effectiveness ratios, efficiency ratios, activity ratios, and growth ratios.

Financial Ratio Analysis

Financial ratio analysis in the APBD (Regional Budget) is done by comparing the results achieved from one period compared to the previous period so that it can be known how the trends occur.

Independence Ratio: a ratio that describes regional dependence on external funding sources,

Effectiveness Ratios: Ratios that describe the ability of local governments to realize planned local revenues compared to targets set based on the real potential of the region.

Efficiency Ratio: A ratio that describes the comparison between output and input or realization of expenditure with the realization of regional revenues.

Activity Ratio: This ratio illustrates how local governments prioritize the allocation of funds in routine expenditure and optimal development expenditure.

Growth Ratio: A ratio that measures how much the ability of the local government to maintain and increase its success achieved from the period to the next period. With the knowledge of growth for each component of the source of income and expenditure, it can be used to evaluate which potential needs attention.

Capital Expenditure

Capital Expenditures are budget expenditures for the acquisition of fixed assets and other assets that benefit more than one accounting period. In article 53 paragraph 4 Permendagri No. 59 of 2006 stated that the Regional Head establishes a minimum limit of capitalization as the basis for imposing capital expenditures in addition to meeting the minimum limits as well as budget expenditures for goods expenditures must provide benefits for an irregular accounting period. Capital expenditures are budget expenditures used in order to obtain or add fixed assets and other assets that benefit more than one accounting period and exceed the limits of the minimum fixed asset capitalization or other assets set by the government. According to Halim (2008: 73), capital expenditure is the expenditure of regional governments whose benefits exceed one budget year and will add assets or regional wealth and then will add routine expenditure such as maintenance costs to the general administration expenditure group.

Regional Economic Growth

Arsyad (2004) mentions economic growth as an increase in gross domestic product (GDP) or gross national product (GNP) regardless of whether the size is greater or smaller than the rate of population growth or whether changes in economic structure occur or not. There are factors that influence the development of facilities and infrastructure, including natural resources, labor, capital investment, entrepreneurship, transportation, communication, composition of the industrial sector, technology, export markets, the situation of the international economy, local government capacity, government spending and support development.

Economic growth is a long-term increase in capacity of the country concerned to provide economic goods to its population, by the advancement or adjustments in technology, institutional and ideological to various demands of the existing situation (Todaro, 2000: 144). Economic growth is defined as an increase in GDP / PNB regardless of whether the increase is greater or less than the level of population growth or even from changes in economic structure (Arsyad, 2004).

Research Hypothesis

Effect of Financial Performance (Independence Ratio, Effectiveness Ratio, Efficiency Ratio, Activity Ratio, and Growth Ratio) on District / City Capital Expenditures in Bali Province

Financial Performance as measured by regional financial ratios include independence ratios, effectiveness ratios, efficiency ratios, activity ratios (routine expenditure ratios and development spending), and growth ratios (PAD, total income, routine expenditure and development). With good performance, the government will be able to carry out infrastructure and facilities and infrastructure needed by the state, which is reflected in the capital expenditure made by the government. Large capital expenditure is a reflection of the number of infrastructure and facilities being built. The higher the regional financial performance, the more infrastructure and facilities are built which means the optimal capital expenditure of local governments. the more sources that produce, the more results will be. This is in accordance with the previous definition, where PKKD means "increasing the achievement of a work in the area of regional finance which includes the budget and realization of PAD and Capital Expenditures by using financial indicators determined through a policy or statutory provisions from one budget period to the next budget period ". The research conducted by Sularso and Restianto (2011) resulted in regional financial performance influencing capital expenditure. Likewise, the research by Ardini and Handayani (2011) also found that regional financial performance as measured by regional financial ratios has a significant effect on capital expenditure.

H1: Financial Performance ((independence ratio, effectiveness ratio, efficiency ratio, activity ratio, and growth ratio) have a significant effect on Capital Expenditures

Effect of Capital Expenditures on Economic Growth in Districts / Cities in Bali Province

In the local government, the construction of facilities and infrastructure has a positive effect on economic growth (Yustikasari and Darwanto, 2007). The fundamental requirement for economic development is the level of development capital development that is balanced with population growth. Yustikasari and Darwanto (2007) examined the Influence of Economic Growth with Capital Expenditures and found that between capital expenditure and economic growth there was a positive but insignificant relationship. Other research was also carried out by Situngkir (2009) which resulted in an insignificant influence in examining the effects of Economic Growth, PAD (Own-source Revenue), DAU (General Allocation Grant), and DAK (Special Allocation Fund) on the allocation of Capital Expenditures. Mallick (2013) and Adi (2006) state that there is a positive and significant influence between capital expenditure and economic growth.

H2: Capital expenditure has a significant impact on economic growth.

Effect of Financial Performance (Independence Ratio, Effectiveness Ratio, Efficiency Ratio, Activity Ratio, and Growth Ratio) on Economic Growth in Districts / Cities in Bali Province

Financial Performance as measured by regional financial ratios include independence ratios, effectiveness ratios, efficiency ratios, activity ratios (ratio of routine expenditure and development expenditure), and the ratio of PAD growth, total income, routine expenditure and development). This performance improvement is expected to be able to optimize absorption which is seen with optimal development spending which of course is the aim of increasing regional economic growth. Like the research conducted by Lucky (2013), it was found that performance had an effect on economic growth after going through capital expenditure. Financial performance affects the allocation of capital expenditure, capital expenditure affects economic growth and regional financial performance affects indirect economic growth (Sularso and Restianto: 2011)

H3: Regional financial performance (independence ratio, effectiveness ratio, efficiency ratio, activity ratio, and growth ratio) have a significant effect on economic growth.

RESEARCH METHODOLOGY

Fiscal decentralization will provide improved services in various sectors, especially the public sector. This increase in public services has consequences which is where the government needs to provide a greater expenditure allocation for this purpose. Fiscal decentralization will provide greater authority in regional management in improving regional financial performance (independence ratio, effectiveness ratio, efficiency ratio, activity ratio, and growth ratio) so that the regional government can optimize the allocation of total expenditure so that it is expected to improve the regional economy. Problems arise when the region has been able to improve its performance but still has not been able to optimize its absorption so that an increase in economic growth is not achieved. The problem arises when inappropriate allocations in capital expenditure and revenues are not optimal in the source of income received by the government so that of course it will have an impact on the economic growth of the region. This research was conducted in all regencies / cities in Bali Province. The variables used in this research are the Regional Financial Performance (Independence Ratio, Effectiveness Ratio, Efficiency Ratio, Activity Ratio, and Growth Ratio), Capital Expenditures, and Economic Growth.

Regional Financial Performance

The calculation of each regional financial performance ratio is as follows:

Ratio of regional financial independence based on APBD

$$\text{Independence Ratio} = \frac{\text{Locally-generated Revenue}}{\text{Central/Local Government Fund Assistance}}$$

Effectiveness Ratio based on APBD (Regional Development Budget)

$$\text{Effectiveness Ratio} = \frac{\text{Realization of Revenue from Local Revenues}}{\text{The PAD target is determined based on the region's real potential}}$$

$$\text{The Efficiency Ratio is measured by:} = \frac{\text{Realization of Expenditure}}{\text{Realization of Revenue}}$$

Activity Ratios can be formulated as follows:

$$\text{Ratio of routine expenditure to APBD} = \frac{\text{Total routine expenditure on APBD}}{\text{Total APBD}}$$

$$\text{Ratio of development spending to APBD} = \frac{\text{Total development expenditure on APBD}}{\text{Total APBD}}$$

Growth ratio, calculating by:

$$\text{Percentage of PAD (Own Source Revenue) growth} = \frac{\text{PAD year p} - \text{PAD year p-1}}{\text{PAD year p-1}} \times 100$$

$$\text{Percentage of Total Revenue Growth} = \frac{\text{Revenue year p} - \text{Revenue year p-1}}{\text{Revenue year p-1}} \times 100$$

Percentage of regional routine expenditure growth

$$= \frac{\text{Routine Expenditure year p} - \text{Routine Expenditure year p-1}}{\text{Routine Expenditure year p-1}} \times 100$$

Percentage of growth in development spending

$$= \frac{\text{Development spending year p} - \text{Development spending year p-1}}{\text{Development spending year p-1}} \times 100$$

Capital Expenditures

Capital expenditures represent budget expenditures for the acquisition of fixed assets and other assets that benefit more than one accounting period. Capital expenditures include capital expenditure for the acquisition of land, buildings and buildings, equipment and intangible assets indicators of capital expenditure variables are measured by:

Capital Expenditures = Land Expenditures + Equipment and Machinery Expenditures + Building and

Building Shopping + Road, Irigrasi, and Network Spending + Other Fixed Asset Expenditures

Allocation of Capital Expenditures= $\frac{\text{Capital expenditure}}{\text{Total Capital Expenditure}} \times 100$

Economic Growth

Regional economic growth is the GDP or GRDP without considering whether the increase is greater or less than the level of population growth or whether there is a change in the economic structure. GRDP growth rate is the growth rate from year to year which is calculated by the formula: $G = \frac{\text{GDRBt} - \text{GDRBt-1}}{\text{GDRB t-1}} \times 100$

Sampling

The sampling technique of this study uses census method. The data studied is data on the realization of APBD and GRDP from 2011 to 2016.

Data Sources

The type of data used in this study is secondary data. Data sources from APBD realization report documents and GRDP obtained from the website of the Director General of Regional Government Financial Balance through the website www.djpk.depkeu.go.id and BPS. From the report on the realization of the APBD and GRDP in 2011-2016 data can be obtained regarding the data needed in the calculation of regional financial performance, the capital and data needed in describing economic growth (GRDP). The data collection method of this study was carried out using the documentation method. Data were obtained from data published by the Central Bureau of Statistics of the Province of Bali.

The analysis technique used in this study includes descriptive statistics and inferential statistics through inner model testing (PLS) and hypothesis testing (SEM). Descriptive statistics are intended to provide an overview or description of a data which is seen from the mean (mean), standard deviation, variance, maximum, minimum, sum, range, and so on (Ghozali, 2011). In this study the variables used are the Growth of Regional Financial Performance, Capital Expenditures, and Economic Growth (GRDP).

In this research, data analysis used Partial Least Square (PLS) approach. Evaluation of the inner model is done by looking at the magnitude of the structural path coefficient, and also the t test value of the statistics obtained by the bootstrapping method. To test the hypothesis and produce a suitable model (fit), this study uses a variance based or component based approach with Partial Least Square (PLS). If the structural model to be analyzed meets the recursive model and the latent variable has indicators that are formative, reflexive, or mixed, then the most appropriate approach to use is PLS. In PLS the structural model of the relationship between latent variables is called the inner model, while the measurement model (reflexive or formative) is called the outer model.

ANALYSIS AND RESULTS

Results of Model Evaluation Analysis

The analysis model used in this study is a structural equation model with Partial Least square (PLS) approach. The use of PLS as an analytical method requires several steps of structural equation modeling (see Figure 1).

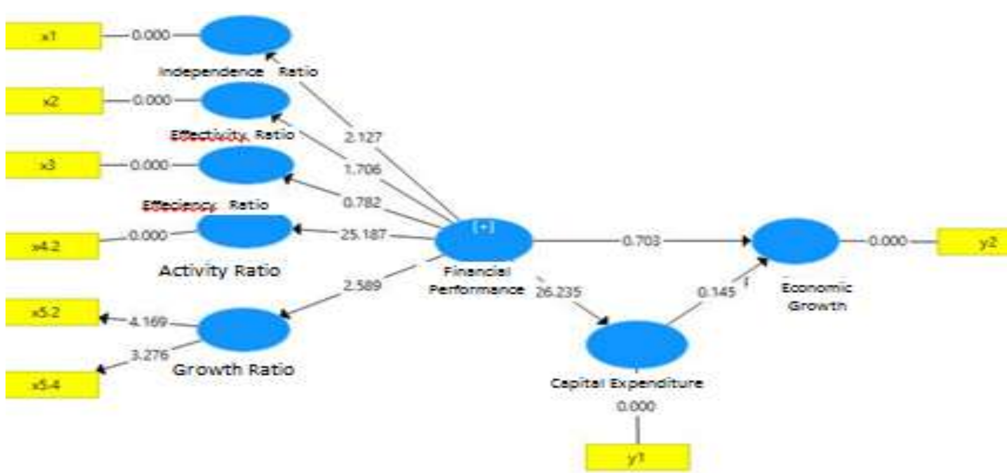

Figure 1. Model of Structural Equation Testing

Source : PLS Output

Furthermore, a model evaluation (Goodness of Fit) is carried out. The measurement model (outer model) with a reflective indicator is evaluated with convergent and discriminant validity of the indicator and composite reliability for the overall indicator. Outer models with their formative indicators are evaluated based on the size and significance of their weight values. Instead the structural model (Inner model) is evaluated by looking at R-Square (R2) in the equation between endogenous latent variables by calculating the predictive-relevance (Q2) value and then seeing the path in the inner model.

Measurement Model Results (inner model)

Inner model evaluation can be seen from the R-square value (R2) on the equation between endogenous latent variables by calculating the predictive-relevance (Q2) value with the formula: Q2 = 1- (1-R12) (1-R22) ... (1- Rp2). If Q2 is greater than 0, the model is interpreted quite well, meaning that it is able to explain the phenomenon of regional economic growth variables at the value of Q2. R-square values of endogenous latent variables are presented in Table 1.

Table 1: R-square (R2) Value Endogenous Latent Variable

Latent Variables	R2
Regional financial performance:	
Independence Ratio	0,225
Effectiveness Ratio	0,117
Efficiency Ratio	0,053
Rasio of Activity	0,770
Ratio of Growth	0,302
Capital Expenditure	0,788
GDRD	0,071

Based on Table 1, it can be explained that the influence of regional financial performance variables on capital expenditure is 78.8%. These results can be interpreted that regional financial performance variables are able to explain the variance in capital expenditure by 78.8% or capital expenditure is influenced by regional financial performance by 78.86%. The R-square value of 0.071 is also found in regional economic growth. This value means that the variables of regional economic growth can be explained by the variables of regional financial performance and capital expenditure of 7.1% or regional economic growth influenced by regional financial performance and capital expenditure of 7.1%

Hypothesis testing

Hypothesis testing is done by using t-test (t-test) on each path of influence between the independent variable and the dependent variable, as well as between the independent variables with the dependent variable mediated by intervening variables. The results of the calculation of the path as a whole can be seen in the path coefficients and the total effects. Testing the hypothesis in this study using the PLS Smart 2.0 M3 structural model. The results of testing this research hypothesis can be seen in Table 2 below:

Table 2: Hypothesis Testing Result

Hypothesis	Original Sample	T-Statistics	P Value
BM → PE	0,045	0,145	0,884
KK → BM	0,888	26,235	0,000
KK→ PE	0,225	0,703	0,482

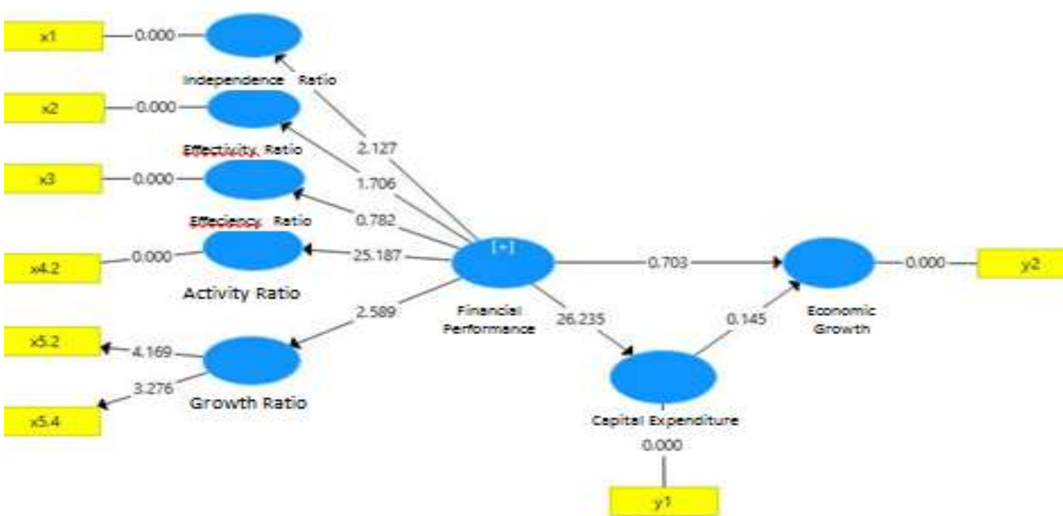

Figure 2: Hypothesis Test Path Chart

DISCUSSION OF RESULTS

Effect of Regional Financial Performance on Capital Expenditures in All Regencies / Cities of Bali Province

Based on the results of the above research, the regional financial performance directly has a positive and significant effect on capital expenditure. The results of the study are in line with the research conducted by Novianto and Hanafiah (2015), Fitri (2013) and Ardhini and Handayani (2011). This significant influence indicates that regional financial performance is a benchmark for the region as a budget allocation (capital expenditure).

Effect of Capital Expenditures on Regional Economic Growth in All Regencies / Cities of Bali Province

Based on the results of the above research, capital expenditure does not have a significant effect on regional economic growth. The results of this study are in line with the research conducted by Lucy (2013), Nurudeen and Usman (2010). This insignificant result shows that the allocation of capital expenditure for district / city regional governments does not determine regional economic growth. Lucky (2013) stated that it turns out that each region has its own economic growth pattern, so that no matter how the government prepares budget absorption for capital expenditure, it cannot affect regional economic growth.

Effect of Regional Financial Performance on Regional Economic Growth in All Regencies/ Cities of Bali Province

Based on the results of the above research, the regional financial performance has no significant effect on regional economic growth. The results of this study are in line with research conducted by Ani and Dwirandra (2014). This insignificant result shows the financial performance of the district / city does not determine regional economic growth. Increased financial performance indicates that financial management in all regencies / cities is improved better, but the inequality of development in all regions in the province of Bali has resulted in different economic growth in all districts / cities in Bali Province.

Table 3: T-test Result of Regional Financial Performance Indicator

Hipotesis	Original Sample	T-Statistics	P Value
KK → RKM	0.474	2,127	0,034
KK → REFV	-0,342	1,706	0,089
KK → REFS	0,230	0,782	0,435
KK → RAKTV	0,877	25,187	0,000
KK → RPTBM	0,550	2,569	0,010

Based on Table 3, it can be seen that the one that builds regional financial performance significantly is the independence ratio, activity ratio, and growth ratio. This can prove that local governments in all regencies / cities in Bali concentrate more on improving regional financial management, and the variables that support economic growth are less attention by the government, and this also has to do with the absence of influence of capital expenditure on economic growth. Local governments pay more attention to increasing income rather than paying attention to factors that support economic growth.

CONCLUSION AND SUGGESTIONS

This study aims to examine and explain the relationship of regional financial performance to capital expenditure and economic growth. From the results of the analysis it was found that the relationship between regional financial performance was significant to capital expenditure while supporting the results of research conducted by Novianto and Hanafiah (2015), Fitri (2013) and Ardhini and Handayani (2011). The relationship of capital expenditure to regional economic growth is not significant. This is because each region has the autonomy to determine the proportion and allocation of regional expenditures, the needs of different balancing funds, the demographical facts typical of each region and the priority scale of development in each region. Research is supported by Lucy (2013), Nurudeen and Usman (2010).

The relationship of regional financial performance to economic growth is not significant. This is because economic growth is a macro variable that involves more the role of government policies, inflation factors, political conditions, and the investment climate. In the regional micro context, mapping and management of regional potential that has not been maximized and policies are not on target. This research is in line with Ani and Dwirandra (2014).

This research provides insight into the management of financial performance so that the theoretical implications enrich the body of knowledge, especially in relationships that are not significant between variables. In managerial implications of local government or financial management stakeholders based on priority scale, sustainable development, mapping of regional potential and strengthening the informal sector, and optimizing regional revenues.

Based on the results of the discussion, it can be suggested: in increasing budget absorption, the regional government should pay attention to its performance. Improved performance will be able to increase the absorption of local government budgets in terms of independence ratios, effectiveness ratios, efficiency ratios, activity ratios, and growth ratios.

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