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# The Role of Budget Ratcheting as Moderating the Effect of General Allocation Funds on Capital Expenditures: Implications for Economic Growth and Public Welfare

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***Abstract***
*This study aims to examine the effect of general allocation funds on capital expenditures, examine the effect of budget ratcheting on the relationship between general allocation funds and capital expenditures, examine the effect of capital expenditures on economic growth, and examine the effect of economic growth on public welfare. This study uses districts/cities in East Nusa Tenggara Province for the 2015-2019 period. The data analysis technique used purposive sampling method. The results showed that the general allocation funds had a positive effect on capital expenditures. The results of the moderating effect research show that budget ratcheting strengthens the relationship between general allocation funds and capital expenditures. while the results of this study indicate that capital expenditure does not significantly affect economic growth, and the results of this study also show that economic growth does not significantly affect the public welfare.*

***Keywords:*** *general allocation fund, capital expenditure, budget ratcheting, economic growth, public welfare*

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## I. Introduction

Welfare is a standard for a society to be in a prosperous situation or condition. Public welfare can be measured by several indicators, namely, the Human Development Index (IPM) and Poverty. The human development index indicator is measured to see the success of the Development and Welfare of an area. There are four factors in the HDI which are benchmarks for the welfare of an area, namely, life expectancy at birth which measures health, literacy rate is used to measure the adult population, average length of schooling is used to measure education, and purchasing power is used to measure education. measure the standard of living.

Based on data from the Central Statistics Agency (2019) related to the HDI of the Province of East Nusa Tenggara (NTT) from 2015-2019, it shows that the HDI of the people of East Nusa Tenggara in 2015 was 62.67% categorized as medium or medium. In 2016 NTT HDI was 63.13%. This means that in 2016 there was an increase of 0.46%. In 2017 the HDI of NTT increased again by 63.73%, thus an increase of 0.6% compared to 2016. In 2018 the HDI of NTT was 64.39% and in 2019 the HDI of NTT reached 65.23%. This shows that NTT's HDI in 2019 has increased by 0.84% compared to 2018. However, based on observations, there are several districts with a percentage of the district's HDI <60, namely Sabu Raijua, East Manggarai, Malaka, Sumba Tengah, Rote Ndao and Alor. This shows that the human development index in NTT represents the welfare of the people in NTT. Efforts to improve the public welfare of NTT by realizing quality economic growth.

The realization of this quality economic growth is carried out through a policy of expanding employment opportunities to reduce the unemployment rate, as well as increasing productive investment in various economic sectors. The neo-classical theory explains that economic growth depends on the accumulation of supply of production factors in this case population, labor and capital accumulation and what needs to be considered is the level of technological progress.

The economic growth rate of the province of NTT based on BPS data shows that for five years it has been fluctuating, namely experiencing different increases and decreases in economic growth. The cause of this fluctuation can be identified through regional income which is dominated by balancing funds and other legitimate income. An area with a low regional financial independence growth rate will have a low regional economic growth rate. On the other hand, an area that has a high growth rate of regional financial independence is expected to have high regional economic growth (Aryantini, 2017).

In the preparation of local government budgets, economic growth affects the budget and of course has an impact on the welfare of the community. This shows that an increase in economic growth is expected to

follow an increase in people's welfare. Economic growth, which is followed by an increase in people's welfare, can be done if capital expenditures are allocated properly.

Oka et al. (2015) explains that sustainable development in the public sector requires improving public facilities and infrastructure. Government investment includes renovation of education, health and other supporting facilities. The fundamental requirement in economic development is the level of capital procurement that is balanced with the population. Thus, the addition of public sector service facilities and the improvement of public sector service facilities by local governments are expected to spur economic growth in the regions.

The capital expenditure budget is one of the budget posts to support public service facilities and is used to add public facilities. According to PMK No. 102/PMK.02/2016, capital expenditures are expenditures to pay for the acquisition of fixed assets or other assets or add value to fixed assets and/or other assets that provide benefits for more than one year in the accounting period and exceed the minimum limit for capitalization of fixed assets. other determined by the government. Based on capital expenditure data for the Province of NTT at the Regency/City level in 2015-2019, it shows that the budget at the Regency and City level fluctuates. From 2015 to 2016 in all regencies/cities. However, in 2017 and 2018 there was a drastic decrease in the capital expenditure budget. A drastic decline occurred in all regencies and cities in the province of NTT.

The central government implements public financial management policies by delegating authority to each region called regional autonomy and fiscal decentralization. Regional autonomy and fiscal decentralization are implemented as drivers of development and equity at the local government level so that the aspirations and needs of the people in the regions become development priorities. On the basis of the above intent, the issuance of regulations governing local government finances, namely Law number 32 of 2004 concerning regional government, Law number 33 of 2004 concerning financial balance between central and regional governments and Law of the Republic of Indonesia number 23 of 2004. 2014 concerning regional government which is a legal guideline for the implementation of fiscal decentralization. The above regulation regulates the points of delegation of authority to regional governments as well as funding for the implementation of these powers so that regional governments can manage existing sources of regional income to finance development activities in the regions so that they do not rely solely on general allocation funds (GAF). According to Sidik (2002) explains that the role of general allocation funds is very significant because regional spending regulations are dominated by the amount of GAF compared to local revenue (PAD). General allocation funds are funds sourced from APBN revenues which are allocated with the aim of equitable distribution of financial capacity among regions and to fund regional needs in the context of implementing decentralization.

General allocation funds and capital expenditures have a very important role in increasing economic growth and public welfare in NTT Province. As we all know that the general allocation fund is a transfer fund from the central government to the regions which aims to reduce horizontal inequality between regions and efforts to equalize the needs of each region. Thus, the general allocation fund is deemed necessary to support the regional income. Related to the intent, there are expenditures or expenditures issued by each region. The expenditure in question is capital expenditure. Capital expenditures are expenditures made for the improvement of public facilities and infrastructure, as well as the construction of public service facilities.

Based on data from the Directorate General of Fiscal Balance (DJPK) of the Ministry of Finance for 2015-2019, the realization of the general allocation fund for the province of NTT is in line with the target and even exceeds the target and the general allocation fund budgeted for 2015-2019 has increased every year. This shows that the government's efforts to implement decentralization have been going well. However, in the preparation of local government budgets, the determination of general allocation funds tends to continue to increase, of course it will have a negative impact on the principle of regional independence as a form of implementation of regional autonomy.

Local government budgets are prepared annually, requiring adjustments during the current fiscal year with the aim of including changes in priorities in the face of unexpected events and the emergence of a surplus from the previous year (Anessi-Pessina et al. 2012). There is a change in the budget due to an increase in the revenue or expenditure budget or vice versa and the initial estimate. Furthermore Forrester et al. (1992) explained that budget changes in the budgeting process are things that are often done so that they become an important factor in local governments. An important factor in local government that needs to be considered in budgeting is the existence of budget ratcheting. Abdullah & Junita (2016) explained that budget ratcheting is a behavioral bias carried out in the preparation of local government budgets which is shown through the accumulation of the previous year's revenue realization plus the rate of budget growth. Lim (2011) explains that a positive income variance will be associated with future income. Meanwhile, negative income will not be affiliated with future revenue budgets. Thus it can be seen that the budget that occurs in budget ratcheting is a budget that has a positive variance.

East Nusa Tenggara Province based on NTT Provincial APBD report data sourced from the Directorate General of Fiscal Balance of the Ministry of Finance in 2015-2019 shows that there is a budget ratcheting phenomenon in 2015-2019. This is known through the budget ratcheting formula approach that was carried out in Abdullah & Janita's research in 2016. The following is data on the budget ratcheting phenomenon.

**Table 1.2**
**NTT Province Budget Ratcheting Data**
**Year 2014- 2019**

| No. | Year | *Budget Ratcheting* |
|---|---|---|
| 1. | 2015 | Rp 3.282.668.641.900 |
| 2. | 2016 | Rp 3.909.020.861.396 |
| 3. | 2017 | Rp 4.722.266.028.826 |
| 4. | 2018 | Rp 4.859.554.863.590 |
| 5. | 2019 | Rp 5.246.170.004.698 |

Source: Processed Data, Djpk.depkeu.go.id

Through observations on the NTT province's budget ratcheting data, the phenomenon of budget ratcheting has increased every year. The largest increase in budget ratcheting occurred in 2016 and 2017 when compared to 2015, 2018, and 2019.

Abdullah & Nazry (2015) in their research found that the remaining previous budget had a significant influence on the expenditure allocation. Thus, the remainder of the previous budget and changes in the budget in the past year are added to make changes to the current budget year. Budgeting behavior that follows the previous year's budget size method is called budgeting ratchet (Lee & Plummer, 2007).

In other words, the effect of budget ratcheting on the budgeting process of government organizations is an explanation for the growth of the budget each year. Budget growth that occurs every year more or less simply follows the classic norm, namely "the realization of the previous year's budget plus a certain growth rate" (Marlowe, 2009). This has implications in the form of a tendency for overproduction of public goods and services, effort reduction, and using the budget for non-essential activities towards the end of the fiscal year (Lee & Plummer, 2007).

## THEORY REVIEW AND HYPOTHESES DEVELOPMENT

### Agency Theory

Agency theory is a concept that explains the contractual relationship between the principal and the agent. Jensen & Meckling (1976) explained that the conflict of interest between the agent and the principal gives rise to information asymmetry. The agent as the party managing the organization has more comprehensive information than the principal. Agency theory has been massively used in both the private and public sectors. This theory is used in analyzing the relationship between principals and agents in public sector budgeting (Abdullah & Nazry, 2015). Furthermore, Marvanti & Praptoyo (2017) explained that the agency relationship in government involves the executive, legislative and community/public. The view of Einsenhardt (1989) explains that there are 3 basic human assumptions to explain agency theory, namely, (1) the tendency of humans to be more selfish (self interest), (2) humans have limited thinking power related to views in the future (bounded). rationality) and humans always avoid risk (risk averse).

### General Allocation Funds

According to Law no. 33 of 2004, the general allocation fund is a number of funds sourced from the APBN which is channeled with the aim of equitable distribution of financial capacity among regions to fund regional needs in the implementation of decentralization (Law No. 33 of 2004). The distribution of funds to regions through profit sharing based on producing regions tends to create inequality between regions by taking into account the needs and potential of the region. The DAU allocation for regions with large fiscal potential but small fiscal needs will receive a relatively small general allocation of funds. On the other hand, regions that have small fiscal potential but large fiscal needs will receive relatively large general fund allocations. With a view to seeing the ability of the APBD to finance regional needs in the context of regional development, which is reflected in the general revenue of the APBD minus personnel expenditures. According to Bastian (2003: 160), "general allocation funds are balancing funds in the context of equitable distribution of financial capacity among regions". Meanwhile, according to Halim (2002: 160), "General allocation funds are funds originating from the state revenue and expenditure budget (APBN) which are allocated with the aim of equitable distribution of regional financial capabilities to finance their expenditure needs in the context of implementing decentralization.

### Capital Expenditures

According to the regulation of the Minister of Home Affairs Number 13 of 2006 article 53 concerning regional financial management guidelines, it defines that capital expenditure is a APBD budget expenditure used for the procurement and development of tangible fixed assets that have a benefit value of more than 12 months as used in government activities. This government activity is in the form of land, equipment and machinery, buildings and structures, irrigation roads, networks and other fixed assets. According to Badrudin (2017: 63)

explains that capital expenditure is an investment in the form of procurement or purchase of assets that have a useful value of more than 12 (twelve) months, then the assets are used for activities that are economically, socially, and other benefits, so that there are increasing the capacity of public services for the community.

**Budget Ratcheting**

According to Bevan & Hood (2006) explains that the form of self-interest in the agency's view occurs when there is a phenomenon carried out by managers to achieve a target more easily by utilizing the superiority of the information they have. The information used in determining targets for the following year can be identified by looking at the target information and performance achievements in the previous year. The basis for determining the next target is deemed necessary to refer to favorable information. This is known as Budget Ratcheting.

**Public welfare**

Smith (2006) explains that the size of the community is said to be prosperous and have a decent life when there is an increase in the ability and equity of basic needs such as food, housing, health, and protection, an increase in the standard of living, income level, decent education, increased respect for cultural values. human values, and expanding economies of scale and the availability of social and individual and national choices.

**Human Development Index**

According to the Central Bureau of Statistics, the Human Development Index (HDI) is a measurement of the comparison of education life expectancy with living standards for all countries around the world. HDI is used to identify and categorize a country as a developed country, a developing country or an underdeveloped country and to measure the effect of economic policies on the quality of life. If the public service facilities and infrastructure are fulfilled, the community will certainly feel comfortable and be able to run their business effectively and efficiently. Thus, a society with a healthy life and a better life expectancy will be realized in improving the quality of education and the standard of living of the community. HDI is calculated based on a combination of three dimensions, namely the age dimension, the educated human dimension, and the decent standard of living dimension. Dimensions of HDI can be measured as follows; First, the age dimension in living a healthy life can be measured by life expectancy. Second, the educated human dimension is measured by the level of adult reading and writing ability and the length of education in elementary school, junior high school, and high school. Third, the dimension of a decent standard of living as measured by purchasing power parity and adjusted real per capita expenditure. HDI achievements are categorized as follows; if HDI 80 then it is categorized as very high. If the Standard 70≤IPM<80) is categorized as high, if the HDI is 60≤IPM<70 it is categorized as moderate and if the HDI<60 is categorized as low. Thus, the concept of public welfare in the HDI has included aspects of health and education along with aspects of clothing, food and housing into a unit with income levels. (Badrudin, 2017:159).

**Economic growth**

Economic growth according to Zulyanto (2010), economic growth is defined as a long-term increase in the ability of a country to provide more types of economic goods to its population. This capability grows with technological progress and the institutional and ideological adjustments it requires. It is further emphasized in the definition that it has three components. First, the economic growth of a nation can be seen from the continuous increase in the supply of goods. Second, advanced technology is a factor in economic growth that determines the degree of growth in the ability to provide various kinds of goods and services to the population. Third, the widespread and efficient use of technology requires adjustments in the institutional and ideological fields so that the resulting innovations can be utilized appropriately. To understand the economic growth in a country, Todaro and Smith (2011) found that there are three main components in the economic growth of each nation, namely capital accumulation, economic growth of occupation and employment and technology.

**Hypothesis Development**

**The Effect of the General Allocation Fund on Capital Expenditure**

Agency theory explains that the agency relationship is a contractual agreement between the principal and the agent (Jensen & Meckling, 1976). It is further explained that the principal contracts the agent with the aim of carrying out some services in their interest by delegating authority to the agent in making decisions. The legislative "opportunistic" behavior occurs in the position as the principal. As a principal for the executive, the legislature includes its personal interests in making policies that seem to have become an agreement between the legislature and the executive, but this policy benefits the legislature in the long run. This long-term policy not only benefits individuals, but also benefits institutions. Policies proposed by the legislature are difficult to reject by the executive because the legislature has discretionary power. In addition, opportunistic behavior also occurs

in executives as agents. As an agent for the legislature, the executive includes his personal interests in the preparation of the budget. This is because the executive has a stronger source of information related to the budget, which is indicated by the executive knowing clearly the conditions of the bureaucracy and regional administration. Therefore, there is a conflict of interest between the legislature and the executive.

With fiscal decentralization, the central government has high hopes for local governments to be able to manage resources so that they do not depend on general allocation funds. In some regions, regional spending policies are more dominated by the role of GAF than PAD itself (Sidik, 2002). So that the central government transfer funds to the regions, in this case the GAF, are used for expenditures for each regional government. So the local government is very pessimistic about setting a regional plan. However, they are more optimistic in setting a spending plan so that the general allocation fund received tends to be larger. Budgeting for general allocation funds can of course be said to be a process in determining revenue targets which should be carried out by taking into account and considering the rules in the object of income in particular by referring to laws, government regulations and regional regulations and it is deemed necessary to pay attention to data on potential transfer funds from the center to the regions. in this case the general allocation fund. Research conducted by Adyatma & Oktaviani (2015) proves that general allocation funds have a positive effect on capital expenditures. Also, the results of another study conducted by Supadmi & Sugiarthi (2014) found that general allocation funds had a positive effect on capital expenditure. In this regard, in Tuasikal's (2008) research, it is also known that general allocation funds have a significant effect on capital expenditures. Based on the theory and research results described, the following hypotheses can be drawn up:

**H1**: The General Allocation Fund has a positive effect on Capital Expenditure.

**Budget Ratcheting affects the relationship between General Allocation Funds and Capital Expenditures**

Agency theory Jensen & Meckling (1976) explains that there is an agreement between the principal and the agent. This is indicated by the principal delegating responsibility for decision making to the agent. So that it is easier for agents to make decisions that will always benefit the agent himself. In addition, the principal must also have opportunistic behavior by including his personal interests in setting policies. This cannot be rejected by the agent because the principal himself has discretionary power. In the public sector, in this case the local government, the principal is referred to as the legislature and the executive as the agent. The conflict of interest in the agency perspective that occurs in local government is when the legislature and executive want to prioritize their personal interests rather than prioritizing common interests so that there is information asymmetry. The executive as an agent, has more sources of information related to the condition of the bureaucracy and regional administration which will certainly affect the budget preparation process, while the legislature has the authority to set policies that seem to represent the community but are more concerned with their personal interests.

Budgeting for general allocation funds can of course be said to be a process in determining revenue targets which should be carried out by taking into account and considering the rules in the object of income in particular by referring to laws, government regulations and regional regulations and it is deemed necessary to pay attention to data on potential transfer funds from the center to the regions. in this case the general allocation fund. Local governments often experience bias and errors in determining the budget so that the revenue budget is sometimes determined to be higher or lower than the proper fiscal capacity. Voorhees (2010) emphasizes that this condition occurs because of the efforts of politicians in regulating policies with the intention that policies can be used for certain purposes. Marlowe (2009) further explains that there is a tendency for a large budget to be an incentive for the executive to set a target that is lower than the proper fiscal capacity. The condition of high dependence occurs in almost all local governments in Indonesia, of course, local governments need good regulations related to regional financial management. Efforts to increase the target to a certain level from the previous year's income variance will give a good signal for the government to increase spending in the following year. Marlowe (2009) confirms this argument that the conditions described above are referred to as budget ratcheting.

Research conducted by Abdullah & Janita (2016) proves that budget ratcheting moderates the relationship between regional income and expenditure. Research conducted by Sari et al. (2020) states that budget ratcheting strengthens the relationship between local revenue and regional expenditures. Also, the results of research conducted by Chatherine & Mulyani (2020) prove something different, namely that budget ratcheting weakens the relationship between local revenue and regional spending. The results of this study support the agency problem in the APBD when the budget proposer and the person who approves the budget proposal have personal interests, then they are included in the budget or moral hazard. Based on the theory and research results described, the following hypotheses can be formulated:

**H2**: Budget ratcheting moderates the relationship between general allocation funds and capital expenditures.

**Effect of Capital Expenditure on Economic Growth**

The government in regulating the economy of a region is manifested in fiscal policy. For the sake of realizing a good regional economy, it is deemed necessary to determine the amount of government revenues and expenditures each year, which is listed in the State Revenue and Expenditure Budget (APBN) for national and Regional Revenue and Expenditure Budget (APBD) for regions. In his book Sukirno (2000) suggests the form of stabilizing prices, output levels and even providing job opportunities as well as motivating economic growth is the embodiment of the objectives of fiscal policy. According to Halim (2007) capital expenditure is one of the government's budget expenditures used to obtain fixed assets or other assets that have benefits for more than one year. The capital expenditures referred to are land expenditures, equipment and machinery expenditures, building and building capital expenditures, road capital expenditures, irrigation and networks. With the improvement of facilities and infrastructure in the area, it will also have an impact on the achievement of economic growth in the area. This is also certainly a hope for local governments through capital expenditures, of course, it will spur the community's economy and people's per capita income.

Syukri & Hinaya's research (2019) found that capital expenditures have an effect on economic growth. In their research, Utami & Indrajaya (2019) proves that capital expenditure has a positive effect on economic growth. This is in line with research by Nurmainah (2013) which shows that capital expenditures have an effect on economic growth. Based on the theory and research results described, the following hypotheses can be formulated:

**H3**: Capital Expenditure has a positive effect on Economic Growth.

**The Effect of Economic Growth on Public Welfare**

The economic situation of a region will certainly be reflected through the economic growth of that region. The improvement of public welfare can also be seen through sustainable economic growth. This indicator is important to know the progress of development for the region in the future. Economic growth can be seen from the increasing number of goods and services (output) produced by a region. This research is devoted to the province of East Nusa Tenggara. Economic growth from an economic point of view is considered by gross regional domestic product (GRDP) which is based on constant prices. GRDP can be interpreted as the sum of the total final goods and services and includes the total added value generated by the region in a period of one fiscal year. The next contributor is the indicator used by Mankiw (2006), in measuring economic growth, namely Gross Domestic Product (GDP). In the context of regional economies, scale often uses Gross Regional Domestic Product (GRDP), which is the total gross added value produced by all regional economic departments.

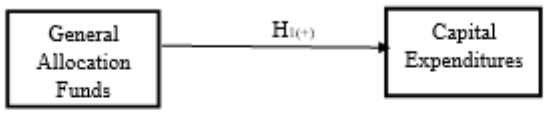
Measuring economic growth using this GRDP, of course, can give an idea related to the total gross added value produced by regional production within a certain time. Furthermore, the development of the value of GRDP is one of the indicators that can be used as a measure to measure the success of the development of a region, or in other words, growth can reflect the economy of a region through the growth of the value of GRDP. Economic growth is also a change in the value of economic activity from one period to another with the same average period, then it can be said that the rate of economic growth must be compared with the annual level of national income. What is meant by the growth of an area is the increase in people's income that occurs in the area and the increase in the overall value that occurs in that area, which is then measured in real value, which means it is expressed at a constant price. If income increases, eating will be explained by an increase in society. Public welfare can be measured by the human development index. The government's role in this case also allows to increase the human development index by realizing the expenditure on public service status (Mirza, 2012). The government's role in the policy of implementing regional autonomy and fiscal decentralization is based on the consideration of a larger region by understanding the requirements and standards of services for the surrounding community. Therefore, the granting of regional autonomy can be expected to encourage the improvement of public welfare in the regions through economic growth. One of the characteristics of modern economic growth is the high growth in output per capita (Todaro 2006). The expected output growth is GRDP per capita. The high increase in output makes changes in consumption patterns to meet needs. This means that with faster economic growth, the growth of output per capita will also be high and there will be changes in consumption patterns, in this case the level of people's purchasing power will also increase. The high purchasing power of the people is one of the comprehensive indicators in the human development index which is referred to as an income indicator. So it can be concluded that the higher the economic growth, the higher the human development index.

The results of Sasana's research (2009) found that economic growth had a significant impact and had a positive correlation on public welfare. Indrajaya & Awandari (2016) in their research proves that economic growth has a significant positive impact on public welfare. Oka et al. (2015) found that economic growth has a positive effect on public welfare. Based on the theory and research results described, the following hypotheses can be formulated:

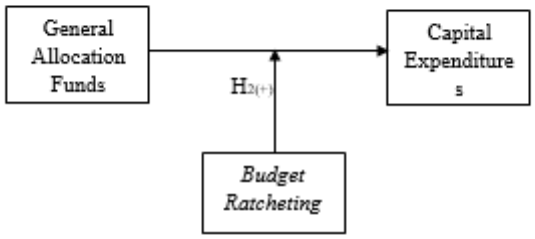
**H4**: Economic Growth has a positive effect on Public Welfare

***Research Model***

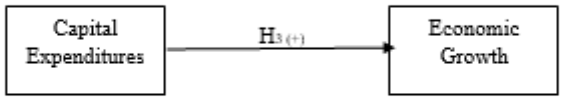
**Model I**



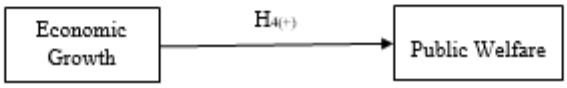

**Model II**




**Model III**




**Model IV**




## II. Research Methodology

**Population and Research Sample**

The definition of the population is the whole of the variables related to the problem under study. The population of this study is all regencies and cities in the province of NTT on the pages of the Directorate General of Fiscal Balance (DJPK) and the Central Statistics Agency (BPS) in 2014 – 2019. Researchers used data for the 2014-2019 period on the grounds of 2015-2019 to measure the variables studied. Meanwhile, 2014 is the base year for measuring the Budget Ratcheting variable. This study selected samples using purposive sampling method, which is a sampling method with several requirements. The requirements used are:

1. Completely available data for the APBD accountability report for the five fiscal years.
2. Not new expansion areas or districts and cities that have been established at least five years earlier.

**Variable Operational Definition**

**General Allocation Fund**

The general allocation fund is a general transfer fund from the central government to the regions in overcoming inequality with the aim of equitable distribution of regional financial capacity to finance expenditure needs in the context of implementing decentralization. The GAF in this study is the amount of the GAF budget for each district/city in NTT Province which can be seen from the balance fund post in the APBD realization report. GAF data has been calculated by the Directorate General of Fiscal Balance (DJPK).

**Capital Expenditure**

Capital expenditures are expenditures issued by the government in the context of developing facilities and infrastructure to meet the needs of the community or in other words development expenditures in the form of building physical investments that have an economic value of more than one year and will result in additional regional assets. Capital expenditures for each district / city can be seen from the heading of the total regional expenditure budget in the APBD realization report. In this study, capital expenditure data is calculated by the Directorate General of Fiscal Balance (DJPK).

**Budget Ratcheting**

Budget ratcheting is a phenomenon of moral hazard behavior by agents in determining performance targets using the previous year's target as a benchmark. Measurement of variables in this study, researchers used the model from (Weitzman, 1980) with the following formula:

$$PADt - PADt_{-1} = \alpha + \beta 1(\text{realization } PADt_{-1} - PAD_{-1}) + e$$

Description :

| | |
|---|---|
| PADt | = local revenue budget in year t |
| $PADt_{-1}$ | = PAD budget in year $t_{-1}$ |
| α | = constant |
| y | = regression coefficient |
| Realization of $PADt_{-1}$ | = realization of PAD in year $t_{-1}$ |
| *e* | = error terms |

**Economic growth**

Economic growth is a presentation of a value that can be known through GRDP which of course will be a benchmark in improving the country's economy (Mirza, 2012). Furthermore, Arsyad (2014), economic growth is a change in GDP per year expressed in percent. The formula for calculating economic growth adopted from research (Badrudin, 2012) is as follows:

$$\text{Economic Growth}_t = \frac{GRDPt - GRDPt-1}{GRDPt-1} \; x\; 100\%$$

**Public welfare**

Public welfare is a condition that reflects the living conditions of the community, which can be seen from the standard of living of the community which is expressed in an indicator unit. The public welfare variable which is used as the latent variable in this study is measured by the human development index (HDI). In this study, the HDI data for the province of NTT which is used as an indicator of public welfare is calculated by the Central Statistics Agency (BPS). If the results of the data processing of the analytical tool meet the expectations of using indicators of public welfare, then the input data will give a higher value to the higher HDI data.

## III. Results And Discussion

**Descriptive statistics**

The statistical results for all research variables are shown in table 4.2.

Table 4.2
Descriptive Statistic

| Variable | N | Min | Max | Mean | Std.Deviation |
|---|---|---|---|---|---|
| CE | 110 | Rp 992.951.633.780 | Rp 452.168.529.736 | Rp 214.000.000.000 | Rp 58.900.000.000 |
| GAF | 110 | Rp 316.115.258.000 | Rp 771.270.719.000 | Rp 528.781.090.000 | Rp 111.000.000.000 |
| EG | 110 | 6,60 % | 14,35 % | 9,37 % | 1,37 % |
| PW | 110 | 53,28 % | 79,55 % | 62,27 % | 4,43 % |
| BR | 110 | -21162,00 | 32142,00 | -0,045455 | 9814,786 |
| GAF*BR | 110 | -Rp1.437.366.103.154 | Rp 2.000.017.802.275 | Rp485.150.351.057 | Rp 538.000.000.000 |

Source: Processed Data, 2021

Description:

CE : Capital expenditure

GAF : General allocation fund

EG : Economic growth

PW : Public welfare

BR : Budget Ratcheting

GAF*BR : General allocation fund*budget ratcheting

The table shows the minimum CE value of Rp. 992,951,633,780 which occurred in Sikka Regency in 2015. The max value of Rp. 452,168,529,736 was found in Kupang Regency in 2016. The mean value of Rp. 214,463,674,900 which was found in East Flores Regency in 2018 and the standard deviation of CE is Rp 58,900,000,000. The GAF has a minimum value of Rp.316,115,258,000 in Sumba Tengah Regency in 2015. The max value of Rp.771,270,719,000 is in Timor Tengah Selatan Regency in 2019. The mean value is Rp.528,781,090,000 in Manggarai Barat Regency. and the standard deviation of the GAF is Rp.111,000,000,000. EG has a min value of 6.60% found in Nagekeo Regency in 2019. The max value is 14.35%, found in Rote Ndao Regency in 2015. The mean value is 9.37% found in Sikka Regency in 2018, and the standard deviation value is 1.37%. PW has a min value of 53.28% found in Sabu Raijua Regency in 2015. The max value of 79.55% is found in Kupang City in 2019. The mean value is 62.57% found in Manggarai Barat Regency in 2018 and the standard value deviation of 4.42%. BR has a min value of -21162.00 found in Sumba Barat Daya Regency in 2017. The max value is 32142.00 which is found in Kupang Regency in 2015. The mean value is -0.045455 found in Ende Regency in 2016; and the standard deviation value is 9814.786. The min value of GAF*BR is -Rp. 1,437,366,103,154 which is found in the Kupang Regency in 2019. The max value is Rp. 2,000,017,802,275 which is found in the Kupang Regency in 2015. The mean value is Rp. 485,150,351,057 which is found in the Regency Sumba Timur in 2018. And, the standard deviation is Rp.538,000,000.

**Classic Assumption Test**

Researchers used the assumption test to obtain a BLUE model. The following is a description of the two tests.

**Multicollinearity Test**

The results of the multicollinearity test using the correlation value between the two independent variables are shown in table 4.3. following.

Table 4.3
Multicollinearity Test

| | BM | DAU | PE | KM | BR | DAU_BR |
|---|---|---|---|---|---|---|
| BM | 1.000000 | 0.428241 | 0.104658 | 0.166429 | 0.266076 | 0.232785 |
| DAU | 0.428241 | 1.000000 | 0.319309 | 0.447003 | 0.045006 | 0.039302 |
| PE | 0.104658 | 0.319309 | 1.000000 | 0.444228 | 0.154473 | 0.196049 |
| KM | 0.166429 | 0.447003 | 0.444228 | 1.000000 | 0.063683 | 0.100765 |
| BR | 0.266076 | 0.045006 | 0.154473 | 0.063683 | 1.000000 | 0.982896 |
| DAU_BR | 0.232785 | 0.039302 | 0.196049 | 0.100765 | 0.982896 | 1.000000 |

Source: Processed Data, 2021

Table 4.3 shows the results of the correlation test between variables. The test results show that there is multicollinearity between several independent variables (correlation value > 0.90). Gujarati & Porter (2009) and Widarjono (2016) explain that the consequence of multicollinearity is that the model is still BLUE (Best Linear Unbiased Estimator) but the model has large variance and covariance. Thus, model testing can still be continued because the model is still BLUE.

**Heteroscedasticity test**

The researcher used White-s heteroscedasticity-consistent variance and standard error to correct the heteroscedasticity problem in order to obtain robust results (robust). Ghozali & Ratmono (2017) explain that the results of the White-s heteroscedasticity-consistent variance and standard error test are an integral part of the hypothesis test results. In addition, Ekananda (2015) explains that one of the improvements to the heteroscedasticity problem is to use consistent variance with White-s heteroscedasticity-consistent variance and standard error.

**Model Testing**

Paired testing is used by researchers to determine a suitable model in testing the panel data regression hypothesis.

Table 4.4
Chow Test

| Significance Value | Main Effect I | Main Effect II | Main Effect III | Moderating Effect |
|---|---|---|---|---|
| Cross-section Chi-square | 0,0053 | 0,0000 | 0,0018 | 0,0058 |

Source: Processed data, 2021

The results of the Chow test in the table are good for the main effect panel data regression model I, for the main effect II, the main effect III, and the moderating effect has a significance of <0.05. This condition means that the panel data regression model that is suitable for the four effects testing is the fixed effect model. Thus, Ha is supported, that is, the fixed effect model is better than the common effect model. Furthermore, the researchers conducted the Hausman test because the results of the Chow test showed a fixed effect model. The results are shown in table 4.5.

Table 4.5
Hausman Test

| Significance Value | Main Effect I | Main Effect II | Main Effect III | Moderating Effect |
|---|---|---|---|---|
| Cross-section Random | 0,2937 | 0,1684 | 0,5940 | 0,6543 |

Source: Processed Data, 2021

The results of the Hausman test for the main effect panel data regression model I, main effect II, main effect III and moderating effect, the significance value is > 0.05. This condition shows the four regression models of this panel data, the effect test is a random effect model. Thus, Ha is supported, that is, the random effect model is better than the fixed effect model. Furthermore, the researcher conducted the Lagrange multiplier test because the results of the Hausman test showed a random effect model. The results are shown in table 4.6.

Table 4.6
Lagrange Multiplier Test

| Significance Value | Main Effect I | Main Effect II | Main Effect III | Moderating Effect |
|---|---|---|---|---|
| Breusch-Pagan | 0,0376 | 0.0000 | 0,0032 | 0,0496 |

Source: Processed Data, 2021

The results of the Lagrange multiplier test for both the main effect panel data regression model I, main effect II, main effect III and moderating effect have a significance value of <0.05. This condition indicates that the panel data regression model that is suitable for the four effects tests is the random effects model. Thus, Ha is supported, namely the random effect model is better than the common effect model. Therefore, the random effect model is a suitable model to test the research hypothesis.

**Hypothesis test**

There are 4 stages of panel data regression testing in this study, namely, the main effect test I, the main effect test II, the main effect test III and the main effect test.

**Table 4.7 Results of Panel Data Regression Hypothesis 1**
**Random Effect Model (REM)**

| Dependent Variable: CE | | | |
|---|---|---|---|
| Independent Variable | Direction | coefficient | Prob. |
| C | + | 103000000000 | 0,0001 |
| GAF | + | 0,211997 | 0,00000 |

| | | |
|---|---|---|
| Prob (F-statistic) | | 0.000016 |
| $R^2$ | | 0,158577 |
| Adjusted $R^2$ | | 0,150786 |

Source: Processed Data, 2021

Table 4.7 shows the output of panel data regression analysis which shows the coefficient and probability values of each variable as well as the results of the F test and the coefficient of determination.. the probability value of the F test is 0.000016 or <0.05. The coefficient of determination is seen from the value of Adj R2. Based on table 4.7, it can be seen that the resulting R2 value is 0.158577 which indicates that the independent variable in this study is able to explain 15.86% of the dependent variable in the research hypothesis, namely capital expenditure. Thus, the model has a poor ability to explain the dependent variable, while the rest by variables other than this research is 84.14% and it can be observed that the CE and GAF variables have a probability value of <0.05 with a positive coefficient direction. This indicates that the general allocation fund has a (+) and significant effect on capital expenditures. Thus, hypothesis 1 is supported.

**Table 4.8**
**Moderation test results (REM)**
**Hypothesis 2**

| Dependent Variable : BM | | | |
|---|---|---|---|
| Independent Variable | Direction | Coefficient | Prob. |
| C | + | 100.000.000.000 | 0,0001 |
| GAF | + | 0,216121 | 0,0000 |
| BR | - | -1876818 | 0,2194 |
| GAF*BR | + | 0,027362 | 0,0047 |
| Prob (F-statistic) | | | 0,000008 |
| $R^2$ | | | 0,219629 |
| Adjusted $R^2$ | | | 0,197543 |

Source: Processed Data, 2021

Table 4.8 is the result of the regression analysis of the moderating variable. Based on the table, it can be seen that the interaction between the GAF and BR variables has a probability value of 0.0047 which is <0.05. Thus, it can be concluded that the budget ratcheting variable strengthens the relationship between general allocation funds and capital expenditures.

**Table 4.9. Panel Data Regression Results**
**Random Effect Model (REM)**
**Hypothesis 3**

| Dependent Variable : EG | | | |
|---|---|---|---|
| Independent Variable | Direction | Coefficient | Prob. |
| C | + | 9,102882 | 0,4517 |
| CE | + | 0,000000000128 | 0,4011 |
| Prob (F-statistic) | | | 0,403008 |
| $R^2$ | | | 0,006484 |
| Adjusted $R^2$ | | | -0,002715 |

Source: Processed Data, 2021

Table 4.9 shows the output of panel data regression analysis which shows the coefficient and probability values of each variable as well as the results of the F test and the coefficient of determination.. Based on table 4.9 above, the probability value of the F test is 0.403008 or > 0.05. Thus, it can be concluded that the model in this study is a poor model. The coefficient of determination is seen from the value of Adj R2. Based on

table 4.9, it can be seen that the value of Adj R2 produced is -0.002715 which indicates that the independent variable in this study is not able to explain the dependent variable in this study, namely economic growth. Thus, the model has a poor ability to explain the dependent variable and it can be observed that the CE and EG variables have a probability value of > 0.05 with a positive coefficient direction. This indicates that capital expenditure has no significant effect on economic growth. Thus, hypothesis 3 is not supported.

**Table 4.10 Panel Data Regression Results**
**Random Effect Model (REM)**
**Hypothesis 4**

| Dependent Variable : PW | | | |
|---|---|---|---|
| Independent Variable | Direction | Coefficient | Prob. |
| C | + | 66,95738 | 0,0000 |
| EG | - | 0,466980 | 0,1968 |
| Prob( F-statistic) | | | 0,195280 |
| $R^2$ | | | 0,015482 |
| Adjusted $R^2$ | | | 0,006366 |

Source: Processed Data, 2021

Table 4.10 shows the output of multiple regression analysis which shows the coefficient and probability values of each variable as well as the results of the F test and the coefficient of determination. Based on table 4.10 above, the probability value of the F test is 0.196280 or > 0.05. Thus, it can be concluded that the model in this study is a poor model. The coefficient of determination is seen from the value of Adj R2. Based on table 4.10, it can be seen that the resulting Adj R2 value is 0.006366 which indicates that the independent variable in this study is not able to explain the dependent variable in this study, namely the welfare of the community. Thus, the model has a high ability to explain the dependent variable and it can be observed that the EG and PW variables have a probability value of > 0.05 with a negative coefficient direction. This indicates that economic growth has a (-) and insignificant effect on the public welfare . Thus, hypothesis 4 is not supported.

## IV. Discussion

**General allocation fund for capital expenditure**

Testing on hypothesis 1 shows the result that general allocation funds have a positive effect on capital expenditures. It can be explained that the higher the GAF obtained by the regions, the higher the capital expenditure will be. Based on the statement above, agree with the research conducted by Abdullah and Halim (2003) which found that general allocation funds have a significant effect on capital expenditure, and also agree with the research conducted by Prakoso (2004) which clearly found that the large amount of capital expenditure was caused by by the amount of general allocation funds received from the central government.

**Budget ratcheting moderates the relationship between general allocation funds and capital expenditures.**

In this study, it was found that there was an effect of budget ratcheting as a moderating variable on the relationship between general allocation funds and capital expenditures. The results of this study explain that the Adjusted R Square value in the first regression test is 0.158577 or 15.85% and the Adjusted R Square value for the second regression test is 0.197543 or 19.75%. The coefficient of the moderating variable is GAF*BR of 0.027362. Thus, it can be indicated that budget ratcheting strengthens the relationship between general allocation funds and capital expenditures. The results of this study are in line with the results of research conducted by Abdullah & Janita (2016) which gives the results of the first regression the R2 value of 0.847 or 84.7% and in the second regression equation it decreases to 0.939 or 93.9%. Therefore, it is concluded that the relationship between PAD and regional spending is strengthened by budget ratcheting as a moderating variable.

**Capital Expenditure on economic growth**

The test results in the study prove that capital expenditure has no effect on economic growth. This is indicated by a coefficient of 0.000000000128, a t-statistic of 0.843043, and a probability of 0.4011 which has a greater significance level (α) of 0.05. This certainly indicates that capital expenditures have no significant effect on economic growth. This is also because in NTT Province there is a special issue of economic growth. This particular economic growth occurred due to uneven development which could be caused by increased spending but was not followed by a decrease in poverty rates in districts/cities in NTT Province. This statement can be proven by the record of the province which has the third highest poverty rate in Indonesia. In addition, there is a

lack of precise policies in the allocation of capital expenditures so that they have not been able to encourage an increase in demand for regional production. This result is in line with Badrudin et al., (2021) research's which proves that capital expenditure has no effect on economic growth so that even though the government's budget policy in this case is capital expenditure, the contribution is large and growing fast, it cannot allocate capital expenditure efficiently so that the GRDP per capita is still low and does not able to drive economic growth

**Economic Growth on Public Welfare.**

The results of this test explain that economic growth has a negative and insignificant effect with a probability of 0.168 on people's welfare. This is also indicated by the coefficient value of -0.466980. The results of this test are not in line with the opinion of Todaro (2006) which states that one of the characteristics of modern economic growth is the high growth of output per capita. The expected output growth is GRDP per capita. From the results of testing hypothesis 4 as shown in table 4.10, it is different from the research conducted by Sasana (2009) which shows that economic growth has a positive effect on public welfare. It can be indicated that the NTT Province, in this case the Regency/City government, when structuring the development of economic output targets, only uses the assumption that the success of economic growth is only described in a certain percentage. This means that if the target is achieved or exceeds the target, it is said that the Regency/City government is successful in managing government activities. In addition, if this is not achieved, the Regency/City government will fail to manage government activities. The results of this study are also in line with research conducted by Badrudin, Dewanti, et al., (2021) which shows that economic growth has no effect on comunity welfare because there is no development carried out by the government to improve the community's economy, which also causes lack of employment. The society tends not to work, and even if there are any development, those are exclusive, which means those development only can benefit society with the capital only.

**Sensitivity Test**

The researcher conducted a sensitivity test by examining the effect of budget ratcheting on the relationship between general allocation funds and expenditures. This sensitivity test is carried out to test the budget ratcheting in the expenditures position. Thus, the researcher will test the effect of budget ratcheting as a moderator in the expenditure position so that it can be seen that whether budget ratcheting will moderate the relationship between general allocation funds and capital expenditures in the expenditure position or not. After testing using Eviews 12, the test results are shown in tables 4.12, 4.13, 4.14, 4.15 below.

**Regression Equation Model**

The regression equation model for testing the budget retcheting on the expenditure position is as follows:

$$\mathbf{GAF = \alpha + \beta 1CE + \beta 2BR + \beta 3CE*BR + \mathit{e}}$$

Description:

GAF = General Allocation Fund
α = Constant
β1... β3 = Regression Coefficient
CE = Capital Expenditure
BR = Budget Ratcheting
e = Error Term

**Hypothesis test**

Hypothesis testing was conducted to analyze whether the moderating variable in this study was able to strengthen or weaken the relationship between the independent variable and the dependent variable. This moderation test is useful for detecting whether the budget ratcheting variable in the expenditure position moderates the relationship between general allocation funds and capital expenditures. The following are the results of the moderation test.

**Table 4.15**
**Moderation Test Results in the Expenditures position (REM)**

| Dependent Variable : GAF | | | |
|---|---|---|---|
| Independent Variable | Direction | Coefficient | Prob. |
| C | + | 35.300.000.000.000 | 0,0000 |
| EC | + | 0,843134 | 0,0000 |
| BR | + | 7,586954 | 0,0430 |

| | | | |
|---|---|---|---|
| EC*BR | - | -0,381448 | 0,0198 |
| Prob (F-statistic) | | | 0,000022 |
| $R^2$ | | | 0,203617 |
| Adjusted $R^2$ | | | 0,181078 |

Source: Processed Data, 2021

Table 4.15 is the result of the regression analysis of the moderating variable on the expenditure position. Based on the table, it can be seen that the interaction between EC and BR variables has a probability value of 0.0198 which is <0.05. However, the direction of the coefficient of determination is negative at -0.381448. This means that the budget ratcheting variable weakens the relationship between general allocation funds and capital expenditures. This shows that in the expenditure position, moral hazard behavior does not occur in the preparation of local government budgets.

Based on the results of the sensitivity test when viewed from budget slack, based on the test results above, it can be concluded that the determination of expenditure tends to be higher than it should be.

## V. Conclusion

The results of this study indicate that the general allocation fund variable has a positive effect on the capital expenditure variable. The larger the allocation of general allocation funds from the central government to the regions, the larger the capital expenditure will be. The budget ratcheting variable strengthens the relationship between the general allocation fund variable and the capital expenditure variable. This shows that in the preparation of the budget for general allocation funds and capital expenditures, the behavior of budget ratcheting strengthens the relationship between budget preparation, in this case general allocation funds and capital expenditures. Thus, hypothesis 1 is supported and hypothesis 2 is also supported. However, in testing the sensitivity related to budget ratcheting on the position of the budget on the relationship between general allocation funds and capital expenditures, the results show that budget ratcheting weakens the relationship between general allocation funds and capital expenditures.

The results of this study indicate that the capital expenditure variable has no significant effect on the economic growth variable. This means that the greater the expenditure of the capital expenditure budget at the Regency/City level in the Province of NTT, it does not have an effect on economic growth. However, the lower the level of economic growth in this case the GRDP of the Province of NTT at the Regency/City level. The variable of economic growth has no significant effect on public welfare. This shows that the low economic growth at the Regency/City level in NTT Province, the lower the level of public welfare in NTT Province at the Regency/City level. Thus, hypothesis 2 and hypothesis 3 are not supported.

## VI. Limitations

There are several limitations that may affect this research. First, the test period may not be too long so that it has not been able to reveal more in the model being tested. Second, data on general allocation funds and capital expenditures are only limited to the total budget.

## VII. Suggestion

Some important things that need to be improved in this research are: a) future research is expected to add variables for special allocation funds and profit sharing funds which are part of the central government transfer funds to the regions and add variables for goods and services expenditures in measuring the budget preparation process. Thus the measurement of the budget preparation and financing process is more complex. b) future research is expected to use a sample of OPD in districts/cities in NTT Province because in the preparation of local government budgets, each OPD will prepare a budget to meet the needs of OPD in this case public service activities.

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