

CHAPTER II

LITERATURE REVIEW

A. Theoretical Framework

1. Foreign Debt.

a. Definition.

Foreign debt is any State revenue either in the form of foreign exchange in rupiah, rupiah or goods and/or services derived from foreign lenders to be repaid on certain conditions (Machmud, 2016). Based on the description in Arsyad (1999), the foreign aid (overseas) intended herein includes government or private sourced assistance. Almost all government assistance has loose (concessional) or soft conditions; ie granted as grants or as loans with low-interest rates and with longer repayment periods than those offered in international private equity markets. In addition, the government also provides commercial loans, including export credits, capital investments (equity), and "hard" loans from the World Bank and regional development banks. These concessional streams are technically called official development assistance (ODA) but are typically known as foreign aid. According to Basri, theoretically, the problem of foreign debt can be explained through the approach of national income. As one source of development financing, foreign debt is required to cover 3 (three) deficits, namely investment savings gap, budget deficit and current account deficit (wibowo, 2012).

b. Theory of Government Foreign Debt.

Theoretically, the problem of foreign debt can be explained through the approach of national income. As one source of development financing, foreign debt is required to cover 3 deficits, namely investment savings gap, budget deficit and current account deficit. The third relationship of the deficit is explained by Basri (2004) in Harahap (2007) using the three gap models theory framework obtained from the national income identity equation, namely:

Expenditure Side

$$Y = C + I + G + (X - M) \dots\dots\dots (1)$$

Where :

Y = GDP

C = Total Consumption of Society

I = Private Investment

G = Government Spending

X = Exports of Goods and Services

M = Imports of Goods and Services

Revenue Side

$$Y = C + S + T \dots\dots\dots(2)$$

Where:

C = Total Consumption of Society

S = Government Saving

T = Government Tax Revenue

If both sides of the national income identity are combined, it will be obtained:

$$(M-X) = (I-S) + (G - T) \dots\dots\dots(3)$$

Where :

(M-X) = Current Account Deficit

(I-S) = Investment Saving Gap

(G-T) = Government Budget Deficit

The relationship between the need for foreign debt and the three deficits is shown using the balance of payments identity:

$$Dt = (M-X)t + Dst - NFLt + Rt - NOLT \dots\dots (4)$$

Where :

Dt = Debt in year 1

(M-X)t = Current Account Deficit in year 1

Dst = Payment of debt burden (interest+ amortization) in year 1

NFLt = Net inflows of private capital in year 1

Rt = Reserves monetary authorities in year 1

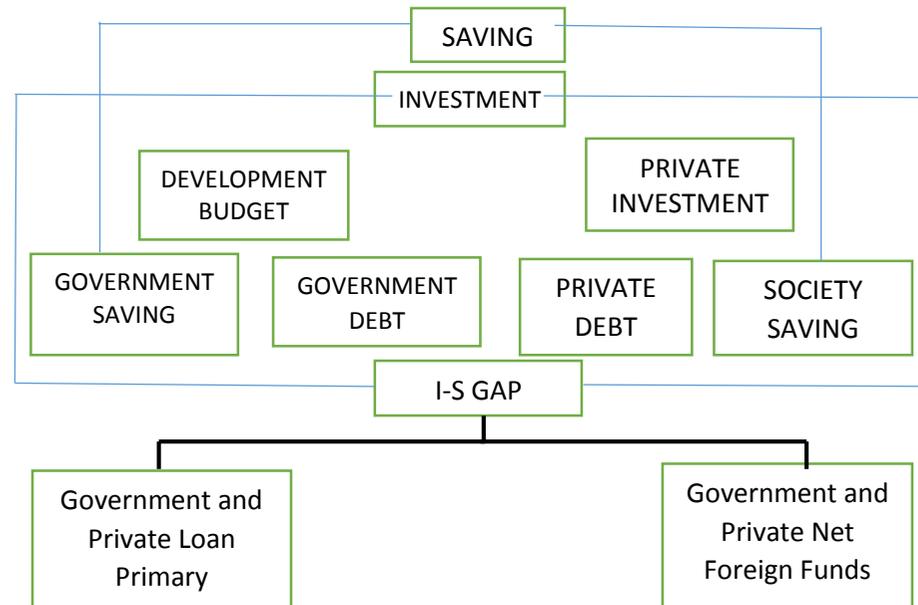
NOLT = Net capital inflows of short-term capital flight and others in year 1.

This equation shows that the Foreign Debt (left side) is used to finance the current account deficit, debt financing, reserves of monetary authority and capital requirements as well as short-term capital flows such as capital flight. If (3) is substituted on (4), then the equation will be obtained:

$$Dt = (I-s)t + (G-T)t + DSt + NFLt + Rt - NOLT \dots\dots(5)$$

The formula (5) shows, in addition to financing the current account deficit, foreign debt is also required to finance the budget deficit of the

government, as well as the saving-investment gap with foreign debt. As the following picture:



Source: Jingham ML (2000) in (Harahap, 2007).

Figure 2.1

I-S Gap

c. Government Foreign Debt Source.

Pasaribu (2012) explained that the sources of foreign debts received by the Government of Indonesia in each budget year in the form of debts derived from:

1) Multilateral Loans.

Multilateral loans are mostly provided in a predetermined loan package, meaning an overseas treaty agreement between the government and international financial institutions to foster some of the multilateral project development projects is mostly from the World Bank, the Asian Development Bank (BPD), the Islamic Development

Bank (BPD) IDB), and several regional and international financial institutions.

2) Bilateral Loan.

Bilateral loans are loans originating from the governments of countries that are members of the Consultative Group on Indonesia (CGI) as an institution that replaces IGGI's position. This bilateral loan is provided to the Indonesian government from:

- a) A soft loan, ie a loan granted based on the results of a CGI hearing.
- b) Loans in the form of Export Credit (Export of Credit) ie loans granted by those States to increase their exports.
- c) Loans in the form of commercial loans, ie credit granted by foreign banks with requirements in accordance with international market developments, for example, LIBOR (London Interbank Offered Rate) and SIBOR (Singapore Interbank Offered Rate) for each type of currency borrowed.
- d) Loans in the form of sale financing installments, ie loans granted by the leasing companies of a certain state to finance contracts between the government and foreign suppliers, as these development contracts cannot be financed from export credit facilities.
- e) Bonds, which are government borrowings by issuing borrower papers with fixed interest rates, whose interest payments are conducted on a regular basis and repayment of loans (principal)

within the stipulated period. In making loans through bonds known 2 types of bonds that can be issued/issued in the capital market, namely:

(1) Public issues (Public Bond Issuance).

The issuance of bonds is conducted through a group of banks that guarantee (underwriter) and sell the bonds to the stock exchange (stock exchange).

(2) Private Placement.

Private bond issuance is limited, not announced to the public. In this case, a sale of bonds is carried out by issuers to a number of banks and institutional investors (insurance companies and pension funds) with the help of a number of banks and institutional investors (insurance companies and pension funds) with the help of a number of a limited underwriter.

- f) Loans in the form of a Sterling Acceptance Facility, which is a loan withdrawal from the bill of exchange. This loan system existed in England since the 17th century. At the beginning of this system is used to obtain credit short-term based on trade transactions conducted. This bill of change can be traded in the sterling acceptance market, thus funds can be obtained before the Bill of Exchange matures.

d. Reasons and Impacts of Foreign Debt.

Based on some theoretical descriptions contained in Saleh (2008), according to Zainulbasri (2000) from the perspective of donor countries there are two important things that underlie and motivate the existence of foreign debtors of the debtor. The second important thing is political motivation (political motivation) and economic motivation (economic motivation) both of which have a very close relationship between one and the other. In addition to these two reasons, Djamin (1993) explained that the existence of moral reasons so that given foreign loans. Hudianto (2005), mentioned that viewed from the theoretical side, government borrowing occurs because of the attraction and encouragement.

In Saleh (2008), theory based on attraction is called the pull theory (loan pull theory) and theory based on encouragement is called loan push theory.

1) Request to borrow.

Based on the theory of attraction of foreign debts, foreign debt occurs because of the demand for such loans from the borrowing country government. There are two categories that underlie the attraction to owe, among others, as follows:

- a) The existence of demand for foreign debts based on sound economic reasons and clearly related to the process of increasing national production capacity.

b) The demand for debts from developing countries without being based on economic calculations (efficient) but by random factors. Factor random is closely related to the behavior of power elites in developing countries, ie corrupt and irresponsible behavior in exploiting foreign debts. In the second category (not through economic considerations) it also includes the demand for foreign debts intended to maintain a high value of exchange rate so that the import of consumer goods increases, and is intended to maintain foreign exchange reserves. These two biases are meant for random categories that are not directly related to increased production capacity.

2) The Urge to Owe From Donor Countries.

According to Mandel in Hudianto (2005) argued that the flow of foreign debts from developed countries to developing countries is not only derived from the demand of borrowing countries but because of the urgent demand of the State debtors with excess petrodollars. From the theory of attraction and encouragement, eventually, loans flow to developing countries. If there is a rational balance between the meaning and impetus then the flow of foreign capital loans can increase national production. However, what happens is that the excess funds are simply thrown away without any economic consideration from the borrowing country. So many things happen that are detrimental to the

borrowing State only because of the interests of certain elites who have a personal interest financed by foreign loans Pasaribu (2012).

2. Exchange Rate.

a. Definition.

According to Krugman and Obstfeld, the exchange rate of each country's currency or exchange rate must be calculated well in conducting international trade transactions to facilitate transactions between countries. The exchange rate is the price of a currency of a State as measured or expressed in other currencies. In making expenditure decisions, the role of exchange rates is very important because exchange rates work for a State in translating prices from different countries into the same language.

Mankiw explains in economics that exchange rates are differentiated to two, namely, nominal exchange rate and real exchange rate. The normal exchange rate is the relative price of the two countries' currencies. Meanwhile, the real exchange rate is the relative price of the goods of the two States stating the degree to which we may trade goods of a State for goods of another State. The real exchange rate is also called the term of trade. Explained by Thobarry, there are two approaches in determining currency exchange rates, namely monetary approach and market approach. In the monetary approach, the exchange rate is defined as the price at which the foreign currency is traded against the domestic currency and the price is related to the supply and demand for money.

b. Changes in the Exchange Rate.

According to Thobarry, currency exchange rate fluctuations can occur in various ways, ie, bias by being officially executed by the government of a State that adheres to a managed floating exchange rate system or also because of the pull of supply and demand forces within market (market mechanism), changes in currency exchange rates occur due to four things:

- 1) Depreciation is the decline in the price of the national currency against foreign currencies, this is due to the attractiveness of the forces of supply and demand within the market.
- 2) Appreciation is an increase in the price of the national currency against foreign currencies, this is due to the attractiveness of the forces of supply and demand within the market.
- 3) Devaluation is the decline in the price of national currency against foreign currency which is done officially by the government of a State.
- 4) Revaluation is an increase in the price of the national currency against foreign currency which is done formally by the government of a State.

c. Exchange Rate System.

The exchange rate system is a policy used by a State to refer to the level of currency value in exchange for the currency of another Country. Some of the exchange rates in the international economy, among others:

- 1) Floating Exchange Rate System (Floating Exchange Rate).

The feature of this system is not convertible to gold, the exchange rate is determined by the market mechanism with or without

stabilization efforts by the monetary authorities. This system is divided into two, namely:

a) Free Floating (Pure).

The exchange rate in this system is wholly determined by market mechanisms without government interference. This system is often called clean floating or pure / freely floating rates because there is no manipulation or determination of the monetary authorities. In this system is not required foreign exchange reserves.

b) Managed or dirty floating rates.

The exchange rate in this system is controlled by the monetary authority in stabilizing the exchange rate at a certain level. Foreign exchange reserves are required in this system because the monetary authority needs to buy or sell foreign exchange in the market to influence the movement of the exchange rate.

2) Pegged Exchange Rate System (Pegged Exchange Rate).

A country links its country's currency to another currency that serves its main trading partner. The intention of tethering in this system is that the currency moves along with its mooring currency (fluctuates following its mooring currency).

3) Crawling Pegs Exchange Rate System (Crawling Pegs).

In this system, a State makes slight changes in its currency value periodically in order to move toward a certain value over a period of time. This system is often used by speculators to earn big profits by

buying or selling the currency before a revaluation or devaluation occurs. The advantage of using this system is that a State may adjust its currency adjustment in a longer period than the tethered exchange rate system. This system can avoid shocks to the economy due to a sudden and sharp revaluation or devaluation.

4) Fixed Exchange Rate System.

In this system, a country announces a certain exchange rate for its currency and maintains this exchange rate by agreeing to buy or sell foreign currency in an unlimited amount at that rate. Exchange rates are usually fixed or allowed to fluctuate within very narrow limits.

Currently almost no country that embraces this system.

d. Theory of Exchange Rates.

1) The Purchasing Power Parity Theory.

Krugman and Obstfeld (1996) explained that this purchasing power parity theory was first proposed by David Ricardo, then reused by Gustav Cassel. The purchasing power parity theory states that the exchange rate between the currencies of two States equals the price-price ratios of the two countries concerned. The domestic purchasing power of a country's currency is reflected in the price level of the State itself (the price level is the money price of a basket or series of goods and services). Thus, purchasing power / PPP parity theory predicts that the declining purchasing power of domestic currency (indicated by domestic price level) will be accompanied by depreciation of its

currency proportionately in the foreign exchange market. In contrast, PPP predicts that the increase in purchasing power of domestic currency will be coupled with a proportional appreciation. The theory is divided into two types, among others:

a) Absolute purchasing-power parity theory.

Salvatore(2014) said in his theory formulates that the exchange rate balance between two currencies equals the ratio of the prices of both countries. In detail:

$$R = \frac{P}{P^*}$$

R represents the exchange rate or spot rate and P and P*, respectively the general price levels at home and abroad. As well as referring to the law of one price, the traded commodity should have the same price (so the purchasing power of both currencies is at parity) in both countries when declared in the same currency.

b) Theory of Relative Purchasing Power Partnership (Relative Purchasing-power Parity).

This theory formulates that changes in exchange rates over a period of time should be proportional to the relative change in price levels in both countries over the same time period.

From both types of purchasing power parity theories, it can be deduced that:

- 1) PPP works well (ie law of one price applies) for each commodity which is often traded with a certain quality but is unfavorable for goods traded simultaneously, and not so good for all goods (which includes various non-merchandise commodities).
- 2) For certain combined levels, PPP theory works very well over very long periods of time (decades), but not so good for one or two decades, and not good overall in the short run.
- 3) PPP works well in cases of pure monetary disturbance and in periods of high inflation, but not very well in a stable monetary period, and is not very good at situations of large structural changes (Salvatore, 2004).

3. Government Expenditures.

a. Definition.

In Prasetya (2012), it is pointed out that society needs a material and spiritual prosperity, the purpose of the sentence is the fulfillment of evolving wants and needs. In the implementation of the fulfillment of these needs used goods and services with various forms including the form of money. The use of money to perform the functions of government is what is meant by government spending. Government expenditure is also defined as the use of money and resources of a State to finance a State or

government activity in order to realize its function in welfare. According to Mangkoesobrot (1994), government spending reflects government policy. If the government has established a policy to purchase goods and services, government expenditures reflect the costs incurred by governments to implement the policy.

Astri (2013) explained that Expenditures in government budget in Indonesia are generally divided into two types, namely routine expenditure and development expenditures (Karimi). Routine expenditures are for purposes such as staff salaries so that they are not for investment but more for governmental operations. The expenditure that can be categorized as public sector investment in development expenditure consisting of a number of sectors. But not all sectors in development spending can be categorized as spending on social or human development.

b. Theory of Government Spending.

Mangkoesobroto (1994) explained the theory of government spending is divided into two groups, namely macro theory and micro theory (Prasetya, 2012).

1) Macro Theory of Government Expenditure.

Government spending in real terms can be used as an indicator of the magnitude of government activities financed by government spending. The bigger and more government activities the greater the government expenditure is concerned. In this theory, government spending consists of three posts. Those are:

- a) Government spending on goods and services purchases
- b) Government expenditure on staff salaries. Employee salary changes have an effect on macroeconomic processes, where changes in staff salaries will affect the level of demand indirectly.
- c) Government spending on transfer payments. Transfer payments are not purchases of goods or services by the government in the merchandise market but rather record payments or direct grants to residents that include eg subsidy payments or direct assistance to various community groups, pension payments, interest payments for government loans to the public. Economically, the transfer payment has the same status and influence as the salary post although the administration is different (Boediono, 1999)

2) Micro Theory of Government Expenditure.

According to Basri (2005), the objective of micro theory on the development of government spending is to analyze the factors that generate demand for public goods and the factors that influence the availability of public goods. The interaction between demand and supply of public goods determines the number of public goods that will be provided through the budget. The number of public goods to be provided will then generate demand for other goods. Basri (2005) also stated that micro theory on government spending can be formulated as follows (Harahap, 2007):

a) Determination of Demand.

$$U_i = f(G, X)$$

Information:

G = Vector of public goods

X = Vector of private goods

I = Individual

U = Utility function

Basri (2005) explained that individual has a demand for public and private goods. However, the effective demand for goods (government and private) depends on budget constraints. Suppose an individual (i) needs public goods (K) as much as GK. To produce goods K as much as GK, the government must arrange a number of activities. For example, the government is trying to improve security. In the execution of efforts to improve the security it is impossible for the government to abolish at all the crime rate. Therefore, the government and society must establish a level of security that is tolerable by the community. A certain level of security can be achieved by various combinations of activities or by using various production functions (Harahap, 2007).

b) Determination of Output Level.

Based on Basri (2005) public goods and services provided by the government are determined by politicians who choose the number of goods and services produced. In addition, politicians also

determine the amount of tax that will be imposed on society to finance the public goods and services in determining the number of goods and services to be provided. The politicians pay attention to the call or the wishes of the people so that people feel satisfied and still choose them as community representatives. The function of the politicians' utility is as follows (Harahap, 2007):

$$U_p = g(x, G, S)$$

Information:

U_p = Utility function

S = Advantages gained by politicians in material form or position

G = Public goods vector

X = Private goods vector

4. Economic Growth.

a. Definition.

According to Samuelson & Nordhaus (2011) in Hatta (2011), economic growth illustrates the expansion of potential GDP or national output of the State. In other words, economic growth occurs when the production-possibility frontier (PPF) of the nation is shifting out. Presented in Hatta (2011), economic growth is a process whereby an increase in real gross national product or real national income. So the economy is said to grow and develop when there is real output growth. In addition, economic growth can also be interpreted by an increase in output per capita. Economic growth illustrates the livability of living standards is measured by real output per person.

b. Theory of Economic Growth.

1) The Neo-Classical Economic Growth Theory.

The increase in foreign debt to finance government spending only raises economic growth in the short term, but in the long run, it will not have a significant impact due to crowding out, a situation where there is overheated in an economy that causes private investment to decrease which will eventually decrease gross domestic product. The budget deficit financed by foreign debt will increase individual consumption. While repayment of debt principal and its repayments in the long term will impose a tax increase for the next generation.

2) The Harrod Domar Growth Theory.

This theory speaks of the use of foreign aid in financing the subsequent development developed by several economists such as Hollis Chenery, Alan Strout, and others in the 1960s and early 1970s. Their thinking as expressed by Chenery and Carter (1973) can be grouped into four basic thoughts:

- a) External sources of funds (foreign capital) can be exploited by developing countries as a significant basis to spur investment and economic growth.
- b) To maintain and maintain a higher growth rate requires substantial changes and reforms in the structure of production and trade.
- c) Foreign capital can play an important role in the mobilization of financial resources and structural transformation.

d) The need for foreign capital will decrease after structural changes occur Pasaribu (2012).

3) The Solow-Swan Economic Development Theory.

The economic growth theory of Solow-Swan states that economic growth depends on increasing the supply of factors of production (population, labor and capital accumulation) and the rate of technological progress. This view is based on a classical analysis, that the economy will continue to experience full employment and the capacity of capital equipment will remain fully used over time. The capital-output ratio (COR) can change and is dynamic. To create a number of specific outlets, commonly used different amounts of capital with the help of different numbers of workers as required. If more capital is used then the labor needed is less, preferably if the capital used is less then more labor which is used. Given this flexibility an economy has unlimited freedom in determining the combination of capital and the workplace to be used to produce a certain level of output (Todaro & Smith, 2011).

5. Government revenue.

a. Definition.

Being explained by Guritno (2009) and Sukanto (2009) that:

1) State Revenue.

Government revenue can be interpreted as government revenue in the widest sense that includes taxes, receipts obtained from the sale of

goods and services owned and produced by the government, government loans, printing money, and so forth.

2) State Revenue and Expenditure Budget.

State income and expenditure budget is the annual financial plan of the Government of Indonesia which is approved by the House of Representatives. The APBN contains a systematic and detailed list containing State revenue and expenditure plans for one fiscal year.

State expenditure is divided into 2, namely:

a) Central government expenditure.

Expenditures used to finance government development activities, both at the central and regional levels. Central government expenditures can be grouped into: personnel expenditures, goods expenditures, capital expenditures, debt interest financing, fuel subsidies and non-fuel subsidies, grant spending, social spending (including disaster management), and other expenditures.

b) Regional Expenditure.

Spending divided into regional governments, to subsequently be included in the regional APBD concerned, includes: revenue-sharing, general allocation funds, special allocation funds, special autonomy funds.

3) State revenue sources.

a) Domestic revenue.

(1) Taxes

(2) Levies

b) Foreign Revenue.

(1) Program Loans.

Loans that are entirely foreign loans that can be disbursed immediately.

(2) Project Loans.

Loans are largely derived from the reactions of project loan commitments in previous years.

4) Journals-Type of State Revenue.

a) Central government revenues.

(1) Financing revenue: banking sector loans, foreign loans, government bond sales, privatization of SOEs, the sale of government assets.

(2) State Revenues and grants: domestic revenues, tax revenues, non-tax state revenues (PNBP), the share of SOE profits, other legal receipts.

(3) Overseas receipts: program loans and project loans.

b. Theory of Government Revenue.

In this case, the researcher using the theory of national income with its calculation method. There are 3 methods to calculate national income, those are:

1) Production Approach Method.

Production approach is additional value which established in a production process.

$$Y = (P_1Q_1) + (P_2Q_2) + \dots (P_nQ_n)$$

Information:

Y= national income

P1= price of goods 1

Q1 = goods 1

Pn= price of good n

Qn = good n

2) Revenue Approach Method.

Revenue approach is an approach which is national revenue earned by accumulating revenue from any kind of production factor which gives contribution to production process.

$$Y = r + w + i + p$$

Information:

Y = national income

r = income from wages, etc

w = net income from rent

i = income from interest

p = income from corporate profit and individual enterprise.

6. The Relationship between Variable.

In this sub-chapter describes the relationship between dependent variable and independent variable.

a. Relationship between variable foreign debt and exchange rate.

The exchange rate is the price of a currency over the currency of a country used to conduct international trade transactions. In the process of borrowing abroad, the borrowing country will follow the currency price of the State lending. When the currency price of the borrowing country depreciates against the currency price of the borrowing country, the debt repayment will be even greater. This is due to the decline in the currency price of the borrowing country. This interrelated relationship also occurs if there is appreciation of the currency price of the borrowing country against the currency price of the lending country. It was explained by Anwar (2011) in Hidayat (2015) that the development of Indonesia's foreign debt during the research period showed a fluctuating development. Based on the estimation of data obtained foreign debt has a negative effect on GDP, *ceteris paribus*. Negative impact is caused by the high amount of installment debt principal and interest that must be paid by the government. Meanwhile, in the total data of foreign debt issued by Bank Indonesia it can be seen that the increase in the amount of foreign debt is followed by economic growth and fluctuating exchange rates.

b. Relationship between variable foreign debt and government expenditure.

Government spending and foreign debt are closely related to each other. In the composition of the APBN, government spending is one of the main indicators in the process of calculating the budget of government expenditure together with the State revenue as a measure from the other side. When the government is unable to reduce its expenditures so that the amount is greater than the revenue, then the State is experiencing budget deficit. When this happens to the economy of a State, then the government must close it with funds from within the country and abroad. Foreign borrowing becomes a very common thing done by a government to close the budget gap. Presented in Hidayat (2015) the development undertaken by the government would require a considerable cost. Government expenditures continue to swell and result in the deficit of the State Budget (APBN). Foreign debt becomes one of the alternative income to finance domestic development. Indonesia's foreign debt can be done by three parties, namely government, Bank Indonesia, and Private. The increasing number of foreign debt indicates that the national economy has not been fully biased by national saving. Swelling of foreign debt will give long-term effects to Indonesia's economic growth. The large burden of debt payments to be borne will hamper national development.

c. The relationship between foreign debt and economic growth.

The making of foreign debt by the government will certainly provide some negative and positive impact on the economy both in terms of fiscal

and monetary. One impact is on economic growth. It is described in (Belawi) that in the short term, foreign borrowing can close the budget deficit, and this is much better than if the deficit of the APBN must be closed by printing new money, enabling the government to implement development with relatively large capital support, without accompanying the effect of increasing the high price level (inflationary effect). Thus the government can make a fiscal expansion to enhance the national economic growth rate. (Belawi) also explained that theoretically in the 1950s and 1960s, in the spirit of the economic duo Harrod-Domar, foreign debt was seen to have a positive impact on economic growth and the increase in community savings as a result of its continued impact. The reason, the flow of foreign debt can increase investment, which in turn increases domestic participation and savings. In theory, foreign debt actually produces positive multiplier effects (multiplier effects) on the economy.

In the 1970s, two other economists Keith Griffin and John Enos in his book "Foreign Assistance: Objectives and Consequences" proved that foreign loans had negative impacts on growth. They propose empirical evidence that foreign debt is negatively correlated to economic growth and increased public savings. Foreign aid has made governments increase spending that reduces the impetus to increase tax revenues and so forth (Hatta, 2011). Todaro (1998) argues that the accumulation of external debt is a common phenomenon. The low domestic savings does not allow for adequate investment, so the governments of developing countries must

withdraw foreign loans and investments. Foreign aid can play a very important role in the State's efforts to reduce its main constraints in the form of foreign exchange shortages, and to enhance its economic growth (Hatta, 2011).

d. The relationship between foreign debt and government revenue.

In the globalization era, development in every side of fields moreover in economic field is growing rapidly. Especially for a developing country like Indonesia that has not been enough in fulfilling its need from its own saving, capital, as well overall kind of income. Pasaribu (2012) stated that every single economic action will lead to some consequences, as what happen when government take assistance from foreign debt to finance its development. In the short term, foreign borrowing can close the budget deficit, and this is far better than if the deficit of the APBN must be closed by printing new money, enabling the government to implement development with relatively large capital support, without the effect of increasing the general price level (inflationary effect). Thus the government can conduct fiscal expansion to enhance the national economic growth rate. Increasing the rate of economic growth means an increase in national income, which in turn allows for increased income per capita society if the population does not increase higher. Increasing per capita income means increasing public prosperity. In the long run, it turns out that foreign debt can cause economic problems in many debtor countries. In addition to the economic burdens that the people must accept at the time of repayment, as

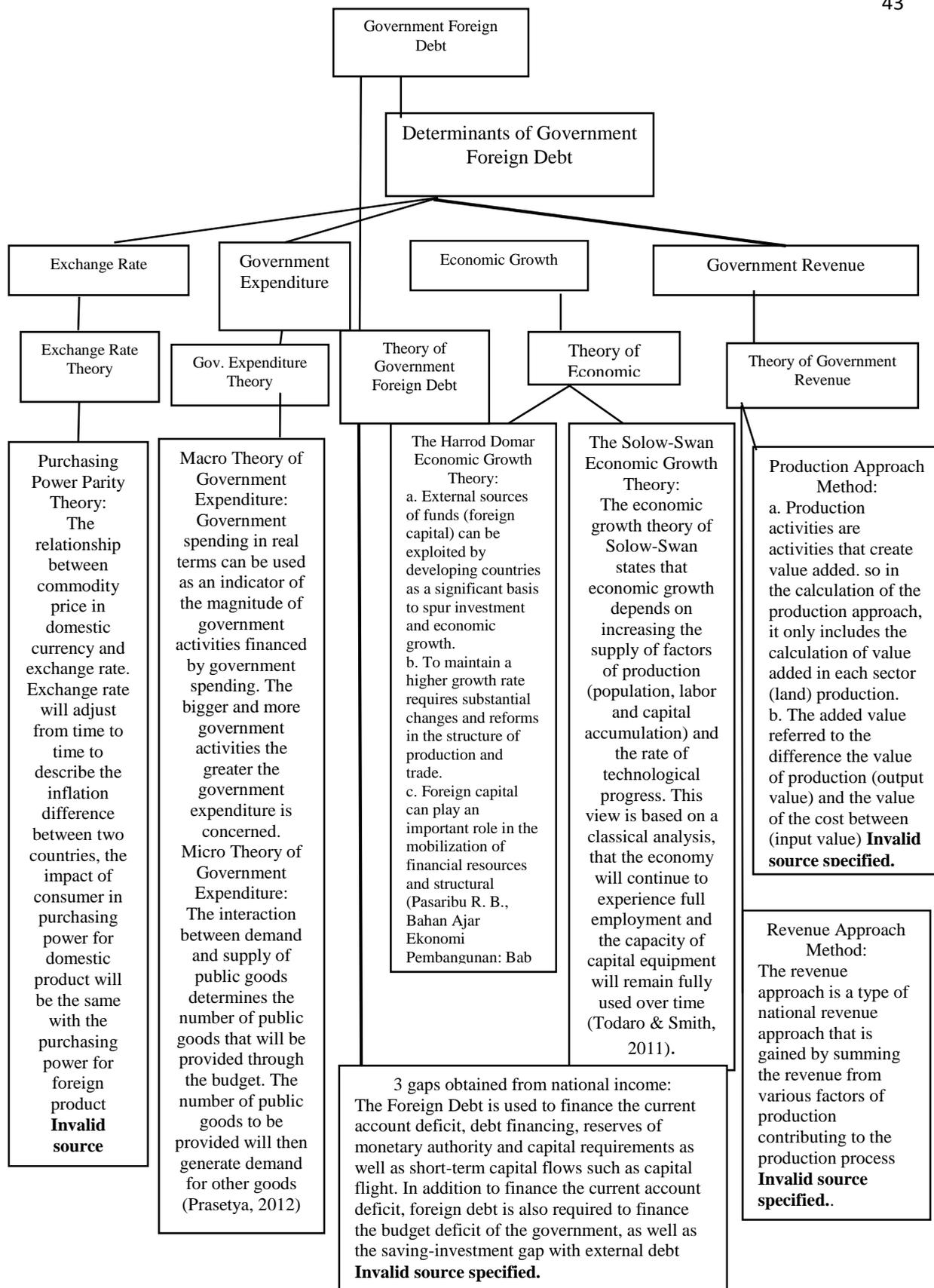
well as the psychological political burden that must be accepted by the country due to its dependence on foreign aid.

Purnama (2014) said that the influence of foreign borrowing on the state budget can be said that the overall foreign debt of the Indonesian government is very influential on the state budget condition. With the considerable amount of foreign borrowing, the Indonesian State Budget will still face pressure to meet the obligation to pay back the principal and interest on loans already and will mature in the future.

Table 2.1

Relationship between Independent Variable and Dependent Variable

No	Variable	Sign	References
1	Indonesia Rupiah Exchange Rate against USD	-	(Hidayat 2015; Al-Fawwaz 2016; Saleh 2008; Free Floating Exchange Rate System)
2	Government Expenditure	+	(Hidayat 2015; Hatta 2011; Harahap 2007; Mah 2013)
3	Economic Growth	+	(Yogi 2017; Neo-Classical Economic Growth Theory)
4	Government Revenue	-	(Harahap 2007; Revenue Approach Method; Pasaribu 2012; Purnama 2014)



Source: processed journal source

Figure 2.2 Theoretical Framework

B. Previous Study

1. Torki M. Al-Fawwaz (2016).

His research entitled "Determinants of External Debt in Jordan: An Empirical Study (1990-2014)". The independent variables used in this study are trade openness, terms of trade, exchange rate, and gross domestic product per capita. While external debt is variable dependent on this research. This study was analyzed using Error Correction Mechanism. The data taken are annual secondary data from the 1990-2014 period. Long-term analysis results show that trade openness has a significant and positive influence on external debt. While GDP per capita has a negative and significant influence on external debt variables in the long term. In the long run, the exchange rate variable has a negative and insignificant effect on the government's foreign debt. In the short-term analysis, all independent variables in the study did not significantly influence external debt except the GDP per capita variables that had a negative and significant influence on the 5% level in lag 2.

2. Samsubar Saleh (2008)

His research entitled "Factors Affecting Foreign Loans and Its Impact on State Budget". Independent variables used in this study include exchange rates, exports, GNP levels, and variable dummy economic crisis 1997. Meanwhile, the dependent variable in this study is Indonesia's foreign debt. The data used in this research is secondary time series data from the 1970-2008 period. This study analyzed methods using Error Correction Mechanism (ECM) and Ordinary Least Square (OLS). The results of this study indicate that in the long run, exchange rate, export, GNP, and dummy variables of 1997 economic crisis have a significant influence

on government external debt. While the variable budget deficit does not show the effect of significant effect on government external debt. Meanwhile, in short-term observation, it was suggested that the dummy variable of the 1997 economic crisis had a significant effect on Indonesia's external debt variable. Other independent variables such as budget deficits, exchange rates, exports, and GNP levels did not have a significant effect on Indonesia's foreign debt during the period of observation.

3. Rehmat Ullah Awan, Akhtar Anjum and Shazia Rahim (2014)

His research entitled "An Econometric Analysis of Determinants of External Debt in Pakistan (Case Study: Pakistan 1976-2010)". The independent variables used in this research are fiscal deficit, nominal exchange rate, and trade openness. Meanwhile, the dependent variable used is external debt in Pakistan. The research was analyzed using Error Correction Mechanism method. The data taken is secondary time series data. Long-term analysis results show that fiscal deficits and external debt have a positive and significant relationship. Other variables such as nominal exchange rate and trade openness also have a positive and significant influence on a certain percentage of external debt. While for short-term analysis shows that fiscal deficit and trade openness have no significant effect and have the negative effect on external debt. For variable exchange rate effect positively and significantly to external debt.

4. Mahindun Dhiani Melda Harahap (2007)

His research entitled "Analysis of Factors Affecting Indonesia's Foreign Debt". The independent variables used in this study are government revenue,

government expenditure, and budget deficit. Meanwhile, the external debt is determined as a variable dependent on this research. The data used in this research is secondary time series data from 1980-2004. This study was analyzed using Ordinary Least Square (OLS) method. The results of this study indicate that domestic income has a negative and significant effect on Indonesia's foreign debt. While the government spending, budget deficit, and foreign debt of the previous year (ULN_{t-1}) have a positive and significant impact on Indonesia's foreign debt.

5. Yogi Afrianto, Evi Susanti Tasri, & Kasman Karimi

His research entitled "Analysis of Factors Affecting Indonesia's Foreign Debt". The independent variables used in this study are a budget deficit, GDP, government expenditure, and rupiah exchange rate against the dollar. Meanwhile, the government's foreign debt is determined as a variable dependent in this research. The data used in this study is secondary data from 2000-2015 published by BPS, BI, and other relevant agencies. This research was analyzed using Multiple Linear Regression Analysis method. The results of this study indicate that budget deficit and GDP have a positive and significant impact on government external debt. While government expenditures have a negative and significant effect on the government's external debt. The rupiah exchange rate against the dollar has a positive but insignificant effect on the government's external debt.

6. I Wayan Gayun Widharma, I Made Kembar Sri Budhi, & A A I N Marhaeni

His research entitled "Indonesia's Foreign Debt: A Study on Influential Factors". Variable independent used in this research is tax revenue, government expenditure, budget deficit, rupiah exchange rate against the dollar, government

foreign debt of previous year, and repayment of government debt period 1981-2010. Meanwhile, the government's foreign debt is determined as a variable dependent on this research. The data used in this study is secondary time series data from 1981-2010 published by BPS, BI, Ministry of Finance, Journal and the results of previous research. This study was analyzed using descriptive analysis method and path analysis or path analysis (extension of multiple linear analysis to assess causality relationship between variables). The results of this study indicate that tax revenue significantly affects the government's external debt through development expenditure and become the dominant variable so that indirectly affect the government's external debt. The budget deficit has no significant effect on the government's external debt through development spending. This is because the size of the government budget deficit is not due to an increase in government spending but is caused by the fuel subsidy policy. The budget deficit has a significant effect on foreign debt through the dollar exchange rate. The repayment of the debt affects the government's external debt through the dollar exchange rate. Development spending has a significant effect on government external debt. The dollar rate has a significant effect on the government's external debt. The government's foreign debt the previous year became the variable that had the most direct and dominant influence on the government's external debt.

7. Moga Tano Jilenga, Helian Xu, Igor-Mathieu Gondje-Dacka

His research entitled "The Impact of External Debt and Foreign Direct Investment on Economic Growth: Empirical Evidence from Tanzania". Variable independent used in this research is external debt and foreign direct investment.

Meanwhile, economic growth is determined as the dependent variable in this research. The data used in this study is the secondary time series data from 1971-2011 published by Index Mundi. This research was analyzed using the econometric method with ARDL model and the bounds test approach of co-integration. The result shows that in the run-up debt promote economic growth in Tanzania. However, foreign direct investment exhibits a negative impact on economic growth. While in the short-run, the results indicate that there is no directional causality between external debts (PD) and economic growth (RGDP) or between FDI_INFL and economic growth (RGDP).

8. Imamudin Yuliadi (2006)

His research entitled "Analysis of Indonesia's Foreign Debt Approach to Macroeconomic Balance". The independent variables used in this research are national income (Y), the exchange rate of Rupiah (ER), government expenditure (G) and the ratio between domestic interest rate and international interest rate (RDNLN). Meanwhile, Indonesia's foreign debt is determined as a variable dependent on this research. The data used in this research is secondary time series data from 1990 quarter I-2004 second quarter published by BPS, BI, ADB, IFS, Ministry of finance and other credible data source information. This study was analyzed using Two-Stage Least Square (TSLS) estimation method. The results of this study indicate that all independent variables in this study did not significantly affect the total amount of government foreign debt except for the rupiah exchange rate variable against US dollar.

9. Gisele Mah, Janine Mukkudem-Petersen, Collins Miruka, Mark A. Petersen (2013)

His research entitled "The Impact of Government Expenditure on the Greek Government Debt: An Econometric Analysis". The independent variables used in this research are government expenditures (government national expenditures), government incomes, net foreign direct investment, and inflation. Meanwhile, Greece government debt. The data used in this study is the annual secondary data from 1976-2011 published by the World Development Indicators, the European Commission Database and the International Monetary Fund. This research was analyzed using Vector Error Correction Model (VECM) and Vector Autoregression Granger causality method to determine the direction of causality. The results of this study indicate that by using VECM gross national government expenditure, gross national income, inflation, and net foreign direct investment affect the Greece general government debt significantly. There is a positive and significant relationship between the gross national government expenditure variable and the inflation of the general government debt. While, it is found the existence of a negative and significant relationship between gross national income and net foreign direct investment to general government debt. Overall variable government expenditure has a significant and dominant influence on general government debt. While the result of VAR Granger causality is the finding of causality from gross national government expenditure and gross national income to general government debt.

10. Yogie Dahhly Saputro and Aris Soelistyo (2017)

His research entitled "Analysis of Factors Affecting Foreign Debt in Indonesia". The independent variables used in this study are a budget deficit, foreign exchange reserves, net exports and foreign debt of the previous year. Meanwhile, Indonesia's foreign debt is determined as a variable dependent on this research. The data used in this research is secondary time series data from 2006-2015 in quarter or quarter. This study was analyzed using Ordinary Least Square (OLS) Analysis method. The results of this study indicate that the budget deficit of revenues, State expenditure, foreign exchange reserves, and foreign debt of the previous government have a positive and significant impact on foreign debt. While net exports have the positive and insignificant effect on foreign debt.

C. Hypothesis

Based on the problems that have been described above, it can be raised several hypotheses in this study, among others:

1. The rupiah exchange rate against the dollar is expected to have a negative and significant impact on Indonesia's government foreign debt in the period of study.
2. Government expenditure is expected to have a positive and significant impact on Indonesia's government foreign debt in the period of study.
3. Economic growth is expected to have a positive and significant impact on Indonesia's government foreign debt in the period of study.
4. Government revenue is expected to have a negative and significant impact on Indonesia's government foreign debt in the period of study.

D. Research Framework

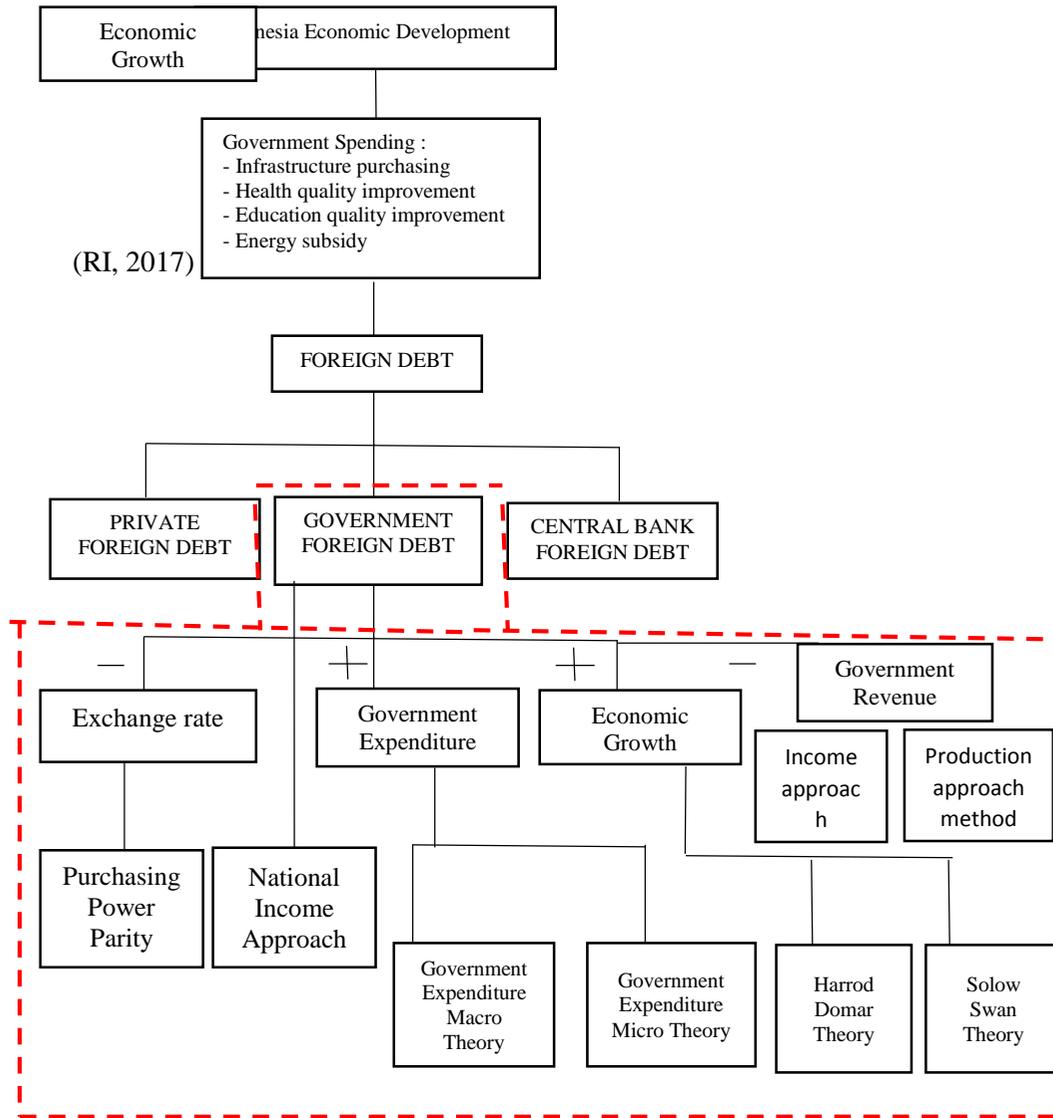


FIGURE 2.3

Research Framework

Information:

- - - - - Research Area

MULTIPLE LINEAR REGRESSION