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INFLUENCE OF INCOME AND INFLATION ON PUBLIC CONSUMPTION IN WEST SUMATRA PROVINCE

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ABSTRACT

This research aims to reveal the influence of income and inflation on public consumption in West Sumatra Province. This research uses a quantitative type of research. The data collection technique in this research uses documentation techniques obtained from Bank Indonesia (BI) and the Central Statistics Agency (BPS) of the Republic of Indonesia which includes data on household consumption expenditure, real income per capita, inflation. The process of processing research data and drawing conclusions was carried out with the help of the SPSS computer program. Overall the independent variables (Per Capita Income and Inflation) have a positive effect on public consumption in West Sumatra Province. Based on the equation, the results show that the variable Per Capita Income has t count (13.056) > t table (1.985) or can also be seen from the significance value of 0.00 < α = 0.05, from this calculation, Per Capita Income has a positive and significant relationship with household consumption. in West Sumatra Province. Likewise, the Inflation variable has a calculated t value of (0.828) > (-1.985), or can be seen from the significance value of 0.828 > α = 0.05, from this calculation, inflation has a significant effect on public consumption in West Sumatra Province.

Keywords: *Income, Inflation, Interest Rates and Consumption*

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INTRODUCTION

People's consumption expenditure patterns are an important factor that needs to be considered when evaluating the evolution of the population's level of economic well-being (Apriyana, 2011). One of the family's economic actions to fulfill various product and service needs is consumption. Therefore, consumption is often used to measure family welfare. Consumption is an integral part of human existence; it serves the purpose of providing basic needs such as food, clothing, and shelter as well as other

purposes. Every human being has consumption expenditure from birth to the end of his life, meaning that every person carries out consumption activities throughout his life. Therefore, consumption activities are very important for human survival (Leunupun et al., 2023).

Apart from GRDP, consumption expenditure patterns can be used as a measure of people's economic welfare, claims Nurhida (2013) (Persaulin et al, 2013). Short-term and long-term economic dynamics are influenced by consumption activities. Consumption affects aggregate demand in the short term and has a significant impact on economic growth in the long term, according to Mankiw (2007). In essence, both non-economic and economic factors have an impact on human consumption needs. Non-economic elements relate to the social and cultural aspects of society, while economic aspects include household wealth, income, and hopes for the household's economic future (Regina, 2022).

According to Keynes' theory, income has an important role in determining consumption, and when disposable income increases, consumption also increases. A person's urge to consume increases as income increases. Conversely, the fewer goods consumed, the lower a person's income. Finding the best way to spend money while still getting maximum satisfaction is the fundamental idea of consumption. Research conducted by Nelwati (2011), whose findings show that income has a positive impact on people's consumption in Indonesia, further strengthens this assumption (Atmaja et al., 2022).

Of the various elements mentioned above, income and per capita income are allegedly among those that have an impact on public consumption. Per capita income is the amount of money a society receives after dividing national income and regional income of the population of a country or region. Sukiro (2012) emphasized that the citizens of a country or region are considered more prosperous and the economy is successful if there is a higher per capita income. Interest rates are another element that influences consumption besides income. Interest rates are also influenced by inflation and savings (Tutupoho, 2019). Mangkoesoebroto (1998) emphasized the existence of a substitution effect between savings and consumption expenditure when the inflation rate increases. A high level of inflation will erode people's purchasing power, especially with regard to domestic production, which will further erode people's confidence in the value of the national currency. As a result, people will spend more money on relatively cheap goods and less money on relatively expensive goods (Arvip, 2015).

Keynes emphasized the existence of a link between national income and consumer spending, where both variables are expressed in constant prices. It is not historical or projected national income that influences consumption, but current national income (Sarlia & Hanum, 2019).

It is evident from national income statistics in many countries, including ours, that household consumption plays an important role in total expenditure. Household consumption accounts for between 60 and 70 percent of national income in most

countries. This includes household spending on things like food and drink, clothing, cars, rent, entertainment, health care, and education (Hasan et al., 2023).

The total amount of finished goods and services produced by a country in a certain period of time, often a single year, constitutes the country's national income. The market value of products and services determines the amount of national income generated. Because not all products created during a certain period are additions to existing products, especially in the case of capital goods, market value is determined in gross value. Everyone has various demands that are influenced by their financial situation (Irawaty & Masloman, 2018). More goods are consumed in proportion to income. On the other hand, fewer goods are consumed in proportion to income. Savings must be utilized because savings will decrease if consumption increases while income remains constant. Considering the circumstances above, it can be said that income has a significant influence on consumption (Dianawati & Mustika, 2016).

A person's consumption is directly correlated with his income. Public consumption expenditure is closely correlated with national income at a macro level. The amount spent on consumption increases as income increases. The practice of saving is also the same. Therefore, savings and expenses will increase with income. Marginal propensity to spend (MPC) is the ratio of new consumption expenditures to additional income. On the other hand, the marginal propensity to save (MPS) is the ratio of the amount of new savings to additional income (Nuryana, 2022).

Central Statistics Agency (BPS) statistics show that in 2023, Indonesia's adjusted real per capita expenditure will be IDR 11.9 million per year. When compared to the previous year which amounted to IDR 11.5 million per year, this amount increased by 3.7%. Moreover, real per capita spending growth in 2023 exceeds the average growth in 2020–2022. The average annual growth in real expenditure per capita during this time is 2.09%. The consumption costs of each Indonesian resident adjusted to purchasing power are called per capita expenditure. The increase in national income over time is also in line with the increase in spending by the Indonesian people. One of the provinces in Indonesia where consumption still contributes more than 50% to GDP is West Sumatra. From 2013 to 2023, the consumption growth of the people of West Sumatra has accelerated. The Central Statistics Agency (BPS) reports that in West Sumatra, real spending per capita in 2023 will be IDR 1,411,823 million. Compared to the previous year which amounted to IDR 1,342,986 million, this number has increased. Interest rates and per capita income are expected to have an impact on increasing consumption by the people of West Sumatra (Ministry of Agriculture, 2021).

LITERATURE REVIEW

Consumption

Suherman Rosyidi defines consumption as the use of products and services that directly meet people's needs. Household expenditure on finished goods and services is referred to as consumption, or more precisely, personal consumption expenditure. N. Gregory Mankiw further stated that expenditure made by households to purchase goods

and services is referred to as consumption. Goods consist of the amount spent by households on non-durable goods such as food and clothing as well as durable goods such as cars and household appliances. Intangible products such as haircuts and health services are examples of services (Economy & Mulawarman, 2022).

The relationship between the amount of household consumption in the economy and national income is characterized by a curve called the consumption function. Mankiw (2007) states that the following equation represents the consumption function:

$$C=C+eY$$

Where Y is national income, e is the slope of marginal consumption, and C is a constant when household consumption is zero (Atmaja et al., 2022).

Mankiw (2007) quotes Keynes's theory, which states that there are several marginal propensity to consume points of view regarding consumption-related issues. Keynes first made the assumption that there was a marginal propensity to consume between zero and one for each additional unit of income. To reduce widespread unemployment, Keynes's policy relied heavily on the willingness of marginal consumption. The relationship between income and consumption provides a fiscal policy multiplier with an indication of the policy's ability to influence the economy. Second, Keynes stated that when income increases, the ratio of consumption to income, or average consumption probability also increases. He anticipated that rich people would save a greater percentage of their income than poor people because he thought saving was a luxury. Third, Keynes stated that the interest rate has no effect on consumption and income is a more significant factor. Keynes stated that there was only a theoretical relationship between interest rates and consumption. He came to the conclusion that spending one's short-term income was largely irrelevant and not very important. The following is a general way to write Keynes's consumption function, based on the following three conjectures:

$$C=\bar{C}+eY, \bar{c}>0, 0<e<1 \quad \text{.....(2,1)}$$

Information :

C = Consumption

Y = Disposable income

$\bar{c}$ = Constant

e = Marginal propensity to consume (Rahmawati, 2019).

Additionally, Irving Fisher created a model in Mankiw (2007) that economists use to test how rational, forward-thinking customers make intertemporal decisions, or decisions that span multiple time periods. Fisher's model removes the limitations and preferences that customers have, as well as the way these factors interact to shape their decisions regarding savings and spending (Irham et al., 2022).

Then, using the Life Cycle Hypothesis, Franco Modigliani in Dombusch (2009) states that people's consumption and expenditure patterns are based on the idea that a person's life cycle period usually influences their consumption receipts and expenditure patterns. According to life cycle theory, people plan their saving and consumption behavior in advance with the aim of distributing their consumption as efficiently as

possible throughout their lives. A person's desire to guarantee consumption in old age is often associated with savings. The following consumption function is derived from life cycle theory:

C=aWR+cYL .....(2,2)

Then, using the Life Cycle Hypothesis hypothesis, Franco Modigliani in Dombusch (2009) states that society's consumption expenditure patterns are based on the idea that an individual's consumption receipts and expenditure patterns are usually influenced by the stages of their life cycle.

In addition, current income Y is the total of two components: permanent income Yp and transitory income YT, according to Million Friedman and the Permanent Income Hypothesis in Mankiw (2007). Where:

Y= YP+YT.....(2,3)

The portion of income that is expected to persist into the future is called permanent income. On the other hand, income that is not expected to last long is called transitory income.

Friedman believes that people's consumption behavior is not adjusted to current income levels, but rather to long-term or permanent consumption prospects. The permanent income hypothesis of consumption behavior, in its most basic version, states that consumption is a function of permanent income, namely:

C=eYP.....(2,4)

where YP represents disposable (permanent) income. Additionally, Friedman's theory clarifies that it is normal expected income—not current income—that determines current consumption. Further manifestations of the consumption function are:

C=f (YP, i) .....(2,5)

where YP is permanent income and i is the real interest rate (Economic Sciences et al., 2014).

Rill Income Per Capita

Mankiw (2006) emphasized that the level of productivity is the main determinant of the gap in per capita income, which measures living standards in rich and poor countries. The amount of goods and services that an employee can produce in one hour is called productivity. Thus, the ability to produce large quantities of goods and services is a prerequisite for a nation's high standard of living. Meanwhile, the Solow model shows that a significant factor influencing the capital stock in steady conditions is the savings rate.

$$\frac{\mathbf{k}^*}{\mathbf{f}\,\mathbf{k}^*} = \frac{\mathbf{S}}{\boldsymbol{\delta}}$$

Where savings are represented by s, the steady state capital stock by k*, and economic output by f(k*). According to the Solow model, if a country allocates most of its income to savings and investment, then the country will have a stable capital stock and a high level of income. On the other hand, a country's stable capital and income will be low if the country only devotes little funds to savings and investment. The same

thing also happens in the Solow model which predicts the growth of a country's per capita income.

According to Keynes' theory, income plays an important role in determining consumption, and higher disposable income means higher consumption. Sukirno (2012) emphasized that a person's tendency to consume increases with the presence of money. Conversely, the fewer goods that must be consumed, the lower a person's income. Therefore, there is a positive correlation between income and consumption (Zakaria, 2016).

Inflation

The process of continuously increasing the price of goods is called inflation. This does not mean that the price increases of various goods occur at the same rate. It is possible that these increases did not occur simultaneously. The important thing is, as time goes by, the average price of goods should continue to increase. Inflation is not the result of a single increase, even if it is a significant one.

Inflation can occur for several reasons, according to Sukirno (2000: 177–178), including:

1. The goal of the economic grouping of people is to increase their income in connection with productivity growth.
2. Unrealistic public expectations, which cause demand for goods and services to grow faster than the amount of additional output that the economy can produce.
3. There are government economic or non-economic initiatives that encourage price increases.
4. Natural forces that have the potential to influence price and production increases.
5. Impact of international inflation: In an open economy, imported commodity prices are influenced by the influence of foreign inflation (Hakim, 2023).

RESEARCH METHODOLOGY

One type of quantitative research was used in this investigation. To enable generalization, quantitative research collects and quantifies data. Then use descriptive statistical methods to examine patterns. involves testing the relationship between variables related to inflation and income using secondary data in the form of cross-sectional and time series data (panel data) (Pratama, 2019). The Central Statistics Agency (BPS) and Bank Indonesia (BI) of the Republic of Indonesia provide documentation methods used in this research, including information on interest rates, real income per capita, inflation and household consumption expenditure. SPSS software makes the process of analyzing research data and drawing conclusions easier.

RESULT AND DISCUSSION

This research uses classical assumption testing to provide certainty that the regression equation derived has robustness and consistency to find out how the

independent components influence the dependent variable. Before testing multiple linear regression, traditional assumptions are first tested using heteroscedasticity, multicollinearity and normality tests. The findings and analysis of the Normality Test are as follows:

Table 1: Normality Test

One-Sample Kolmogorov-Smirnov Test

		Unstandardized Residual
N		11
Normal Parameters[a,b]	Mean	.0000000
	Std. Deviation	38565.62350428
Most Extreme Differences	Absolute	.165
	Positive	.106
	Negative	-.165
Test Statistic		.165
Asymp. Sig. (2-tailed)		.200[c,d]

Source: SPSS Processed Data, 2022

Based on table 1, it can be concluded that the asymp. Sig. (2-tailed) of 0.200, > α = 0.05, meaning that according to decision making using the Kolmogorov-Smirnov test the data has a normal distribution and meets the normality requirements in the regression model.

Next, testing uses the Multicollinearity Test, following are the results and discussion of the Multicollinearity Test:

Table 2: Multicollinearity Test

Model		Collinearity Statistics	
		Tolerance	VIF
1	X1	.645	1.551
	X2	.645	1.551

a. Dependent Variable: Consumption

Source: SPSS Processed Data, 2022

In table 2, the tolerance value of the per capita income variable and the inflation variable is 0.645 > 0.10, while the VIF value for the per capita income variable and the inflation variable is 1.551 < 10, so it can be concluded that there are no symptoms of multicollinearity in the regression model. Next, testing uses the Heteroscedasticity Test, following are the results and discussion of the Heteroscedasticity Test:

Table 3: Heteroscedasticity Test

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-1360305.321	199651.235		-6.813	.000
	X1	82.801	6.342	1.021	13.056	.1000
	X2	3652.491	4410.381	.065	.828	.432

a. Dependent Variable: Consumption

Source: SPSS Processed Data, 2022

In table 3, the test shows that the significant value of the Per Capita Income variable is 0.1000 > α = 0.05, while the significance value of the Inflation variable is 0.432 > α = 0.05. Based on this, it can be concluded that in accordance with the decision making from the Glejser test there is no heteroscedasticity in the regression model.

And then testing the Multiple Linear Analysis, following are the results and discussion of the Multiple Linear Analysis:

Table 4: Multiple Linear Analysis

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-1360305.321	199651.235		-6.813	.000
	X1	82.801	6.342	1.021	13.056	.000
	X2	3652.491	4410.381	.065	.828	.432

a. Dependent Variable: Y

Source: SPSS Processed Data, 2022

Table 4, shows the multiple linear regression equation for each independent variable towards the next variable. The results show that the variable Per Capita Income

has t count (13.056) > t table (1.985) or can also be seen from the significance value of 0.00 < α = 0.05, from this calculation, hypothesis (H1) Per Capita Income has a positive and significant relationship with consumption households in West Sumatra Province. The existence of this positive and significant influence between per capita income and household consumption means that consumption is influenced by per capita income, this condition is caused by an increase in purchasing power. Higher purchasing power will have an impact on increasing consumption. On the other hand, a decrease in per capita income will result in a decrease in consumption because purchasing power will decrease. This is in accordance with what Keynes said in Sukirno (2003: 338) that "a person's consumption is directly proportional to his income." From the results of the analysis it can be seen that the per capita income variable has a positive and significant effect, meaning that if per capita income increases, the value of household consumption automatically increases. stairs will also increase. This is in accordance with the formula Y = C – I – G + ( ) and the amount of exports (X) and imports (M) is 0 (zero), then the model will be Y= C, where if income rises then consumption also rises, and vice versa. The inflation variable has a calculated t value of (0.828) > (-1.985), or it can be seen from the significance value of 0.828 > α = 0.05, from this calculation, the hypothesis (H2) is that inflation has a significant effect on public consumption in West Sumatra. Inflation that increases beyond the set target will cause a decrease in the real value of income, thereby weakening people's purchasing power, especially for domestic production and will cause a decrease in people's consumption. So in the short term, people will reduce their consumption because people with relatively low income levels will prioritize primary consumption and choose to withhold consumption of secondary goods or look for substitutes for goods that are experiencing price increases with goods that are cheaper but have the same benefits.

CONCLUSION

From the results of research carried out using regression testing, using classical assumption testing aims to provide certainty that the regression equation obtained is definite and consistent. The research results show that the test shows a significant value for the Per Capita Income variable of 0.1000 > α = 0.05, so it can be interpreted that Per Capita Income has a positive and significant relationship with household consumption in West Sumatra Province. while the significance value of the Inflation Variable is 0.432 > α = 0.05. So it can be interpreted that inflation has a significant effect on public consumption in West Sumatra.

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