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Analysis of the Influence of Local Government Financial Performance on Economic Growth with Capital Expenditure Allocation as an Intervening Variable in the Regency/City of Sumatera Utara Province

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ABSTRACT

This study aims to examine the effect of financial performance on economic growth with capital expenditure allocation as an intervening variable in Regency/City Governments in Sumatra Utara Province. The study sample consisted of 33 regencies/cities in Sumatra Utara Province. The financial performance variables measured were efficiency, effectiveness, independence, and fiscal decentralization. Data were analyzed using path analysis using the EViews program based on secondary data in the form of panel data sourced from Regency/City Local Government Budget data in Sumatra Utara Province.

The results of the study indicate that efficiency has a positive and significant effect on economic growth, while effectiveness has a positive and significant effect on economic growth. The independence variable has a negative and insignificant effect on economic growth, and the fiscal decentralization variable has a positive and insignificant effect on economic growth. For the indirect effect, the capital expenditure allocation variable only mediates the efficiency variable on economic growth. In contrast, the effectiveness, independence, and fiscal decentralization variables cannot be mediated by capital expenditure allocation on economic growth.

Keywords: *efficiency, effectiveness, independence, fiscal decentralization, capital expenditure allocation, and economic growth.*

INTRODUCTION

The economic development of a region is essentially a series of activities carried out consciously and continuously to realize a better condition together and sustainably. Regional economic development also encourages equitable development in each region so that it can produce equitable development to improve the welfare of the local community. To achieve this goal, various strategies and policies are carried out by the local government. One of the measures of increasing economic growth is by looking at the economic growth of the region. Regional income should be appropriately managed by the local government and utilized optimally for a productive regional budget to improve public services. The community in the education, health, and infrastructure sectors can also feel it. Therefore, an important thing that the local government must implement is the ability to explore the potential of existing

resources in the region and maximize the allocation of all revenues to boost economic growth. According to Todaro (2020), the public sector (government) must be recognized and trusted to play a greater and more decisive role in efforts to manage the national/regional economy. The regional government, as the policy maker in the region, will then prefer to adopt development policies that are adjusted to the characteristics of the potential of the region itself. Of course, the demand for recognizing regional potential can be used as a driver of economic growth for regional development.

Sumatra Utara Province is one of the largest provinces in Indonesia, both in terms of population and national economic contribution, and it has 33 governments, consisting of 15 district governments and 8 city governments. With a variety of natural resources and a strategic geographical location, Sumatra Utara has the opportunity become one of the centers of economic growth in Indonesia as agriculture, plantations (especially oil palm), trade, and processing industry are the potential areas of this province's leading sectors so that it has a reasonably strong economic structure.

One of the indicators of economic development is economic growth, and what reflects the measurement of economic growth of a region in a specific period is the Gross Regional Domestic Product (GRDP) data. Development in all fields that reach all corners of the country requires GRDP data in accordance with the boundaries of the government's administrative areas for development planning, especially in the economic sector, as well as evaluating the results (BPS, 2022). The economic growth of the region is shown by the GRDP growth rate at constant prices (Todaro, 2020). The added value of goods and services is calculated using the prices prevailing in a particular year as a basis. In the BPS publication, the base year used is 2010 (BPS, 2022).

The image below shows the target and realization of the Economic Growth Rate of Sumatra Utara Province obtained from the website of the Central Statistics Agency of Sumatra Utara Province.

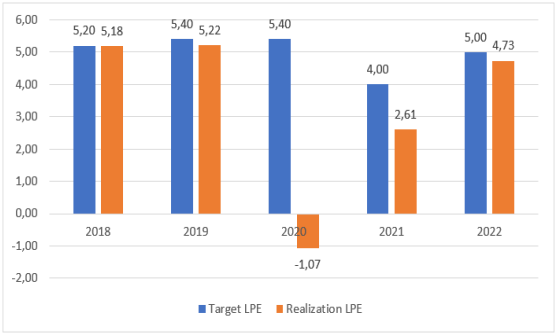


Figure 1. Target and Realization of Economic Growth Rate of Sumatra Utara Province 2018–2022

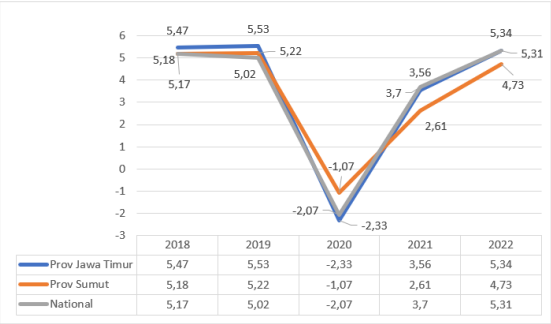
Source: BPS, Sumatra Utara

Figure 1 shows that the economic growth rate of Sumatra Utara Province for the 2018-2022 period each year did not reach the target set in the 2018-2022 Regional Medium-Term Development Plan document. Although in 2018 and 2019, the realization almost reached the target, in 2018, it reached 5.18 percent of the target of 5.20 percent, and in 2019, it reached 5.22 percent of the set 5.40 percent, but the achievement in 2020 was negative. Namely, -1.07 percent of the target of 5.40 percent or economic growth experienced a contraction (minus). If economic growth is positive, it means that the economy is growing. Conversely, if economic growth is negative, it means that the economy is contracting, and if the contractions are consecutive, it is known as a recession (Central Statistics Agency). Likewise, in the following year, in 2021, the target set was 4.00 percent, but the realization only reached 2.61 percent. In 2022, although there was an increase in economic growth, the realization of 4.73 percent was not able to meet the target that had been set, which was 5 percent. It shows that Sumatra Utara Province during 2018-2022 was unable to meet the achievement of the economic growth target that had been set. Based on BPS data, seen from the structure of the Sumatra Utara economy's GRDP, it is supported by the leading sectors of agriculture, plantations, processing industry,

and trade. Palm oil, rubber, and other agricultural commodities are the main sectors that drive the province's GRDP. Nationally, Sumatra Utara is one of the provinces with the largest GRDP in Indonesia, but nationally, it is still below several other large provinces that have the same characteristics. Despite having a large population, Sumatra Utara is still inferior in terms of GRDP per capita compared to other provinces.

As seen from Figure 1, economic growth in Sumatra Utara is still fluctuating. It is not optimal when compared to other provinces that have similar conditions and are also rich in natural resources but have a more stable economic growth rate, such as Jawa Timur. There are several similarities seen in the economic sector between Sumatra Utara Province and Jawa Timur Province, including both having regional potential in the dominant agricultural sector, with primary commodities such as rice, corn, and rubber. In addition, both provinces also have developing processing industries such as rubber, wood, and food processing. Both provinces have made exemplary contributions to national growth.

A comparison of the economic growth achievements of Sumatra Utara Province to the achievements of Jawa Timur Province and national economic growth can be seen in Figure 2.



	2018	2019	2020	2021	2022
Prov Jawa Timur	5,47	5,53	-2,33	3,56	5,34
Prov Sumut	5,18	5,22	-1,07	2,61	4,73
National	5,17	5,02	-2,07	3,7	5,31

Figure 2. Comparison of Economic Growth Rates of Sumatra Utara Province and Jawa Timur Province in 2018–2022

Source: BPS

In 2018, the economic growth of Jawa Timur Province was above the economic growth of Sumatra Utara Province, and both were above national economic growth. When national economic growth decreased from 5.17 to 5.02 in 2019, the economic growth of Jawa Timur Province and Sumatra Utara Province increased, with the economic growth position of Sumatra Utara Province still below Jawa Timur Province. During the Covid period in 2020, both national growth and the two provinces experienced contraction, with Jawa Timur Province at -2.33, lower than Sumatra Utara Province at -1.07 and nationally at -2.07. During the recovery period from Covid 19, in 2021, Jawa Timur Province began to recover to reach 3.56, above Sumatra Utara Province at 2.61, and almost approaching the national economic growth of 3.7. In 2022, the economic growth conditions of Jawa Timur Province returned to being stable before Covid 19, above national economic growth.

Regional financial performance is an essential indicator in measuring the effectiveness of financial management carried out by local governments. This performance includes regional income, regional expenditure, and regional asset management, all of which play an essential role in supporting economic development. Good financial performance allows local governments to finance development programs that have a direct impact on economic growth. Conversely, if regional financial performance is less than optimal, the government's ability to carry out development programs is limited, thus hampering economic growth. Regional financial performance is the ability of a region to meet the needs of its region by managing original regional financial resources to support government public services and regional development (Poyoh et al., 2017).

The financial performance of local governments that affect economic growth can be measured using the effectiveness ratio, efficiency ratio, independence ratio, and fiscal decentralization ratio (Wartiah,

(2023), Darmastuti et al., (2022), Rahayu et al., 2022).

The ability of a region to carry out its duties is categorized as effective if the resulting ratio reaches a minimum of 1 or 100 percent. The higher the effectiveness ratio, the better the performance of the region's ability. It is reinforced by the existence of the Minister of Home Affairs Decree Number 690,900,327 of 1996 concerning Guidelines for Financial Performance and Assessment, which provides criteria for the financial performance effectiveness ratio, namely:

Table 1. Financial Performance Criteria Based on Effectiveness Ratio

Financial Performance Percentage	Criteria
> 100%	Very Effective
90% - 100%	Effective
80% - 90%	Quite Effective
60% - 80%	Less Effective
< 60%	Not Effective

Source: Minister of Home Affairs Decree No. 600.900.327 of 1996

Based on budget and realization data obtained from the Sumatra Utara Central Statistics Agency, the following are the results of calculating the effectiveness ratio of Sumatra Utara Province for 2018-2022.

Table 2. Calculation of the Financial Effectiveness Ratio of Districts/Cities In Sumatra Utara Province 2018 – 2022

Year	Local Government Revenue Budget (Rp)	Local Government Revenue Realization (Rp)	Effectiveness (%)	Criteria
2018	6.505.867.608	5.160.752.592	79,32	Less Effective
2019	6.252.269.893	5.558.200.385	88,90	Effective
2020	6.117.744.327	5.281.007.529	86,32	Effective
2021	6.840.325.070	5.704.020.041	83,39	Effective
2022	6.024.251.041	6.016.935.657	99,88	Very Effective
Average			87,56	Quite Effective

Source: Central Statistics Agency of Sumatra Utara Province

The results of the calculation of the average level of effectiveness of financial management in districts/cities in Sumatra Utara Province in 2018-2022 are shown in Figure 3.

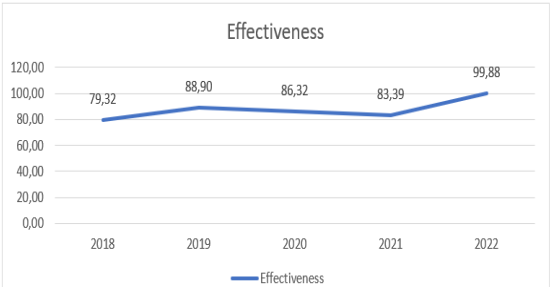


Figure 3. Financial effectiveness ratio of districts/cities in Sumatra Utara Province 2018-2022

Table 2 and Figure 2 of the financial effectiveness ratio of districts/cities in Sumatra Utara Province show that the average effectiveness ratio falls into the effective category. The effectiveness ratio criteria in 2018 were less effective, with the achievement of 79.32 percent, although there was an increase in 2019 to 88.90 percent with effective criteria. In 2020 and 2021, it decreased again and increased again in 2022. When the achievement of this effectiveness ratio is linked to Figure 1 of the target and realization of economic growth, in 2018, the effectiveness ratio fell into the less effective category. However, economic growth in the same year was only 0.02, which is different from the target and realization of growth. Likewise, in 2019, the effectiveness ratio increased into the effective category, but economic growth decreased with a difference of 0.08 between achievement and realization. Even economic growth in 2020 experienced a contraction (minus). In 2021, the achievement of economic growth was very far behind the target, but in the same year, the effectiveness ratio fell into the effective category. It shows inconsistent movement between fluctuations in economic growth and the effectiveness ratio. Research on the effect of the effectiveness ratio on economic growth has been conducted by previous researchers, including Ernawati (2024), Haq et al. (2023), and Saputra et al. (2023), which proves that effectiveness has a positive and significant effect on economic growth. Different results were obtained from research by Nahak et al. (2022), which proved that the effectiveness ratio had a negative and

significant effect on economic growth, while research by Fernanda et al. (2023) stated that effectiveness did not affect regional economic growth.

Regional financial performance can also be calculated through the efficiency ratio. Efficient regional financial performance means that the region can implement development policies in the current year by maximizing the income received so that the income value is greater than the expenditure made by the government.

The Decree of the Minister of Home Affairs, Number 690,900,327 of 1996, concerning Guidelines for Financial Assessment and Performance provides criteria for the financial performance efficiency ratio, namely:

Table 3. Financial Performance Criteria Based on Efficiency Ratios

Financial Performance Efficiency	Criteria
> 100%	Inefficient
90% - 100%	Less efficient
80% - 90%	Quite efficient
60% - 80%	Efficient
< 60%	Very efficient

Source: Minister of Home Affairs Decree No. 600.900.327 of 1996

Based on the data on the realization of income and expenditure obtained from the Sumatra Utara Central Statistics Agency, the following are the results of calculating the efficiency ratio of districts/cities in Sumatra Utara Province in 2018-2022.

Table 4. Calculation of the Efficiency of Local Financial Management of Districts/Cities in the Sumatra Utara Provincial Government in 2018-2022

Year	Revenue Realization (Rp)	Expenditure Realization (Rp)	Efficiency (%)	Criteria
2018	41.632.465.929	41.585.161.516	99,89	Less Efficient
2019	48.136.846.934	44.695.757.009	92,85	Less Efficient
2020	42.332.171.058	41.183.324.504	97,29	Less Efficient
2021	43.764.533.175	45.445.328.446	103,84	Inefficient
2022	45.131.072.079	45.975.453.693	101,87	Inefficient
Average			**99,15**	**Less Efficient**

Source: Central Statistics Agency of Sumatra Utara Province

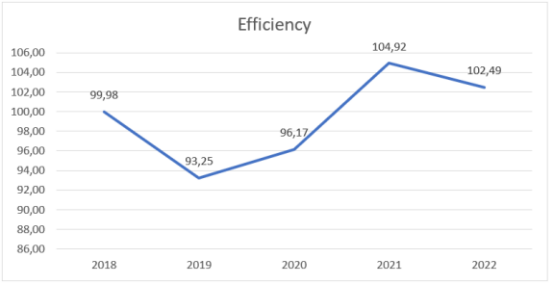


Figure 4. Efficiency ratio of regional financial management of districts/cities in Sumatra Utara Province 2018-2022

Table 4 and Figure 3 show that the average efficiency ratio of Sumatra Utara Province in 2018-2022 is 90-100 percent or less efficient each year, as has happened every year from 2018-2020. Even in 2021 and 2022, it is in the inefficient category because the efficiency ratio is above 100 percent. It means that the management of the financial performance of Sumatra Utara Province in 2018-2022 illustrates that the allocation of spending is greater than its regional income and has not been able to make expenditures more efficient. The achievement of this efficiency ratio is also inconsistent with the movement of economic growth. In 2019, the economic growth of Sumatra Utara Province increased from 2018, but in 2018 and 2019, the financial performance was in the less efficient category. In 2021, the economic growth of Sumatra Utara Province increased compared to 2020. However, in 2021, the efficiency category decreased from less efficient in 2020 to inefficient in 2021, and in 2022, economic growth continued to increase from 2021. However, the position of the efficiency ratio in that year was still in the inefficient category. The inconsistent movement/fluctuation in economic growth with the efficiency ratio is a phenomenon between regional financial performance, as seen from the efficiency ratio to economic growth.

Research on the effect of efficiency on economic growth has been conducted by previous researchers, including Lestari et al. (2019), who stated that financial efficiency has a direct effect on economic growth. It is also supported by research by Haq et al.

(2023) and Saputra et al. (2023), which shows a positive and significant effect of efficiency on economic growth. It is different from research conducted by Ernawati (2024) and Rahayu et al. (2022), which states that efficiency does not have a significant effect on economic growth, and Akbar et al. (2021) and Nahak et al. (2022) prove that efficiency has a negative and insignificant effect on economic growth. Financial independence for regions can be increased by maximizing Local Government Revenue as minimize financial dependence on the central government (Hapsari, 2022). The criteria for assessing regional independence are regulated by the Minister of Home Affairs Decree number 690.900.327 of 1996 concerning Guidelines for Financial Assessment and Performance.

Table 5. Pattern of relations between central and regional governments

Financial capability	Independence Ratio	Pattern
Very Low	0%-25%	Instructive
Low	>25% -50%	Consultative
Moderate	>50% -75%	Participative
High	>75% -100%	Delegative

Source: Minister of Home Affairs Decree No. 600.900.327 of 1996

Based on Local Government Revenue realization data and transfer income obtained from the Sumatra Utara Central Statistics Agency the following are the results of calculating the average ratio of independence of districts/cities in Sumatra Utara Province in 2018-2022.

Table 6. Calculation of the ratio of independence of regional financial management in districts/cities in Sumatra Utara Province in 2018-2022

Year	Local Government Revenue Realization (Rp)	Transfer Income (Rp)	Independence (%)	Pattern
2018	5.160.752.592	28.557.195.356	18,07	Instructive
2019	5.558.200.385	29.901.231.852	18,59	Instructive
2020	5.281.007.529	27.439.229.838	19,25	Instructive
2021	5.704.020.041	35.926.192.205	15,88	Instructive
2022	6.016.935.657	37.224.665.717	16,16	Instructive
Average			**17,59**	**Instruktif**

Source: Central Statistics Agency of Sumatra Utara Province

Table 6 shows that the average regional independence ratio of Sumatra Utara is at the instructive criteria (0-25 percent), namely, the role of the central government is more dominant than the independence of the regional government, and the region is unable to implement regional autonomy. It shows that the level of independence of the districts/cities of Sumatra Utara Province in financing government activities and regional development still relies on external assistance (especially the Central and Provincial Governments) to finance government activities, development, and services to the community.

Table 6, although during 2018-2022 shows the independence ratio of the instructive criteria, from 2018 to 2020, the independence ratio was seen to have increased and fell again until 2022. However, this is seen as the opposite when compared to Figure 1. Economic growth from 2018 to 2020 decreased. Even in 2020, it contracted (minus), while economic growth in 2021 and 2022 continued to increase. This condition shows a fluctuating and inconsistent movement between the movement of the independence ratio and economic growth.

The results of research conducted by Suryaningsih et al. (2022), Azhari et al. (2020), and Zulkarnain et al. (2019) stated that the independence ratio has a positive and significant effect on economic growth. Contrary to this research, namely research by Nahak et al. (2022), Saputra et al. (2023) concluded that regional financial independence has a negative and insignificant effect on regional economic growth. Also, research by Sawitri et al. (2020) produced research that showed that independence does not directly affect regional economic growth.

Fiscal decentralization also affects regional economic growth. Fiscal decentralization allows regions to manage their financial capabilities to finance development in their regions. Decentralization is expected to encourage increased participation, initiative, and creativity in the development of the

community, as well as encourage equal distribution of development results across regions by utilizing existing resources and potential (Mardiasmo, 2018).

The decentralization assessment criteria are determined based on the Decree of the Minister of Home Affairs Number 690.900.327 of 1996 concerning Guidelines for Financial Assessment and Performance.

Table 7. Regional Government Financial Capability Patterns

Financial Ability	Achievements
Very low	0% - 25%
Low	26% - 50%
Medium	51% - 75%
High	76% - 100%

Source: Minister of Home Affairs Decree No. 600.900.327 of 1996

Based on Local Government Revenue realization data and the amount of regional revenue obtained from the Central Statistics Agency of Sumatra Utara Province the following are the results of the calculation of the average ratio of the degree of fiscal decentralization of districts/cities in Sumatra Utara Province in 2018-2022.

Table 8. Calculation of the ratio of fiscal decentralization of regional financial management of districts/cities in Sumatra Utara Province in 2018-2022

Year	Local Government Revenue Realization (Rp)	Total of Local Revenue (Rp)	Fiscal Decentralization (%)	Criteria
2018	5.160.752.592	44.238.962.191	11,67	Very low
2019	5.558.200.385	48.136.846.929	11,55	Very low
2020	5.281.007.529	44.396.666.616	11,90	Very low
2021	5.704.020.041	46.760.362.129	12,20	Very low
2022	6.016.935.657	48.687.466.532	12,36	Very low
Average			**11,93**	

Source: Central Statistics Agency of Sumatra Utara Province

Table 8 shows that the average fiscal decentralization ratio in 2018-2022 of the districts/cities of Sumatra Utara province falls into the very low criteria. It shows that the region's ability to generate its Local Government Revenue is still low compared to the total revenue received. In line with this, the rate of economic growth of the districts/cities of Sumatra Utara province in 2018-2022, based on Figure 1, has fluctuated. It shows an inconsistent movement between the fiscal decentralization ratio and economic growth. It can be seen in Table 8 that the achievement of the decentralization ratio in 2018 was 11.67 percent, and in 2019 decreased to 11.55 percent.

In contrast to economic growth in 2018 of 5.18 percent, it increased in 2019 to 5.22. Furthermore, in 2020, economic growth experienced a contraction (minus) down to -1.07 percent. However, on the contrary, the decentralization ratio increased to 11.90 percent and continued to increase in 2021 to 12.20 percent and in 2022 by 12.36 percent. This increase in the decentralization ratio is not comparable to the increase in the economic growth rate in 2021 by 2.61, almost doubling to 4.73.

The results of research conducted by Rahayu et al. (2022), Pradiatmi et al. (2015), and Sabilla (2014) stated that the ratio of the degree of decentralization has a positive effect on economic growth. It is contrary to the research of Nahak et al. (2022), which stated that fiscal decentralization has a negative and insignificant effect on economic growth. Likewise, research conducted by Lestari et al. (2019) and Sularso (2011) concluded that the ratio of the degree of fiscal decentralization does not affect economic growth.

These various studies indicate the impact of regional financial performance and the need for empirical research on regional financial performance. However, there is inconsistency from several researchers, which may be due to the influence of other variables that were not controlled by previous researchers or due to other variables that mediate, strengthen, or weaken the relationship between regional financial performance and economic growth, namely capital expenditure.

Based on capital expenditure data and total expenditure obtained from the Central

Statistics Agency of Sumatra Utara Province, the following are the results of the calculation of the average capital expenditure allocation for Sumatra Utara Province in 2018-2022.

Table 9. Calculation of the level of capital expenditure allocation for the Sumatra Utara Provincial Government in 2018 - 2022

Year	Capital Expenditure (Rp)	Total of Expenditure (Rp)	Capital Expenditure Allocation (%)	
2018	8.061.164.417	41.585.161.516	19,38	< 30%
2019	8.061.164.417	44.695.757.009	18,04	< 30%
2020	5.511.648.211	41.183.324.504	13,38	< 30%
2021	6.227.859.658	45.445.328.446	13,70	< 30%
2022	8.036.334.966	45.975.453.693	17,48	< 30%
Average			16,40	< 30%

Source: Central Statistics Agency of Sumatra Utara Province

The calculation of the percentage of capital expenditure allocation above shows that during 2018-2022, the districts/cities of the Sumatra Utara Provincial Government have not been able to allocate capital expenditure of at least 30 percent of the total regional expenditure. It indicates that the districts/cities of Sumatra Utara Province have not been able to meet the needs or invest in the form of capital expenditure to improve infrastructure and public services.

Capital expenditure has an evident direct influence because it is one of the direct efforts of the regional government to increase the economic growth of its region. The results of this study are in line with research conducted by Sawitri (2023), Fernanda (2023), Suryaningsih (2022), and Rahayu et al. (2019), which states that capital expenditure has a positive and significant effect on regional economic growth. However, the results of this study are not in line with research conducted by Yunus (2019), which states that capital expenditure does not affect regional economic growth.

The results of the discussion of the background of the problem above show that the influence of regional financial performance on economic growth still varies, as well as the results of previous studies, so researchers are interested in raising the title of this thesis with the title Analysis of the Influence of Regional Financial Performance on Economic Growth with Capital Expenditure Allocation as an Intervening Variable in Regencies/Cities in Sumatra Utara Province.

LITERATURE REVIEW

Economic Growth

Economic growth is a process of increasing output per capita in the long term, so the percentage increase in output must be higher than the percentage increase in population, and there is a long-term tendency for growth to continue (Boediono, 1985). The rate of economic growth is an indicator of the success of a region's development, which can be seen through GRDP and per capita income. Regional financial management plays an essential role in regional economic growth because good management of the budget and public resources can increase investment, infrastructure, and public services that support economic development. It is what will later be a guideline for local governments in realizing economic growth in their regions. Regional development, especially economic development, aims to create changes in people's lives and prosperity, and this is achieved through economic growth (Kuncoro, 2019).

$$\text{Economic Growth} = \frac{\text{PDRBt} - \text{PDRBt} - 1}{\text{PDRBt} - 1} \times 100\%$$

Efficiency

Efficiency is defined as being effective in using existing resources and is related to the concept of productivity in work. Efficiency can be measured by comparing the output produced to the input used.

Measure the level of efficiency to find out how much efficiency is in implementing an activity that has been budgeted and compare it with the output produced using data on spending realization and revenue

realization. The smaller the results of this ratio measurement, the more efficient the financial performance will be, and vice versa (Darmastuti, 2022). The smaller allocation of spending compared to the total regional income indicates that regional financial management tends to be more efficient. The efficiency ratio is a comparison between the amount of costs incurred to obtain income and the realization of income received (Maulina et al., 2019). The formula used in calculating the efficiency ratio is:

$$\text{Efficiency} = \frac{\text{Realization of Local Expenditure}}{\text{Realization of Local Income}} 100\%$$

Effectiveness

The effectiveness ratio is the level of achievement of the implementation of a regional government activity by comparing the realization of revenue with the revenue budget. The effectiveness ratio aims to measure the extent to which the regional government mobilizes revenue revenues according to the target Halim (2013). The effectiveness ratio describes the ability of the regional government to mobilize Local Government Revenue revenues according to the target based on the real potential of each region (Andriyani, 2020). The greater the realization of Local Government Budget revenues against the Local Government Revenue revenue target, the greater the regional financial effectiveness ratio will be and vice versa. If the region has used Local Government Revenue effectively, the regional effectiveness ratio will be higher in meeting the costs of the work program to improve the regional economy and the welfare of the community. The higher the effectiveness ratio, the better the performance of the region's capabilities (Putri, 2020). The formula used in calculating the effectiveness ratio is:

$$\text{Effectiveness} = \frac{\text{Local Government Revenue Realization}}{\text{Local Government Revenue Target}} \times 100\%$$

Independence

Regional financial independence describes the level of regional government's ability to finance its activities in government activities, regional development, regional economic development, and community services (Halim, 2012). The independence ratio describes the level of regional dependence on external funding sources. A region can be said to be independent if it is able to increase its original regional income and does not depend on transfer funds from the center. Financial independence for regions can be increased by maximizing Local Government Revenue to minimize financial dependence on the central government (Hapsari, 2022). The higher the independence ratio, the lower the level of regional dependence on external parties (especially the central government), and vice versa. The independence ratio also describes community participation in regional development. It means that the higher the independence ratio, the higher the community participation in paying regional taxes and levies, which are the main components of Local Government Revenue (Maulina, 2019). The higher the regional financial independence ratio, the higher the regional financial independence (Halim, 2012). The formula used in calculating the independence ratio is:

$$\text{Independence} = \frac{\text{Local Government Revenue Realization}}{\text{Total Transfer Income}} \times 100\%$$

Fiscal Decentralization

Fiscal Decentralization is an essential aspect in the implementation of regional autonomy. It is because fiscal decentralization is the region's ability to increase regional original income through

regional taxes, regional levies, and other sources (Lestari, 2020).

The purpose of fiscal decentralization is to fulfill regional aspirations regarding control over state financial resources, encourage accountability and transparency of regional governments, increase community participation in the regional development process, reduce inequality between regions, ensure the provision of minimum public services in each region and ultimately is expected to improve public welfare in general (Hastuti, 2018).

The authority given to regions to regulate their household affairs is an opportunity and challenge for regional governments. The success of fiscal decentralization applied to a region depends on the ability of the regional government to finance economic activities. Large Regional Original Income (Local Government Revenue) is the ability of regional governments to explore regional potential, which is a source of regional income. The higher the regional government in absorbing regional income sources, the higher the Regional Original Income (Local Government Revenue) obtained. Fiscal decentralization shows the degree of Local Government Revenue contribution to total regional revenue. The higher the Local Government Revenue contribution, the higher the region's ability to implement decentralization (Halim, 2013). The degree of decentralization is calculated using the following formula (BPKP, 2012):

$$\text{Fiscal Decentralization} = \frac{\text{Total of Local Government Revenue}}{\text{Total Regional Revenue}} \times 100$$

Capital Expenditure Allocation

Capital expenditure is a regional government expenditure that has an essential influence on the economic growth of a region and will have leverage in driving the wheels of the regional economy (Kuncoro, 2004). According to Bastian (2006), regional expenditure used for regional development purposes is capital expenditure or development expenditure.

Capital expenditure allocation is an expenditure whose benefits exceed one budget year and can increase government assets, which then increase maintenance costs (Mardiasmo, 2018). Capital expenditure allocation refers to the process of determining and using funds for investment in long-term assets owned by an entity, such as physical infrastructure, production facilities, and human resources. This concept involves allocating available financial resources to provide long-term benefits to the entity concerned. Through proper capital expenditure allocation, local governments can direct their investments to optimize resource use and promote sustainable economic development.

$$\text{Capital Expenditure Allocation} = \frac{\text{Capital Expenditure}}{\text{Total Capital Expenditure}} \times 100\%$$

Framework

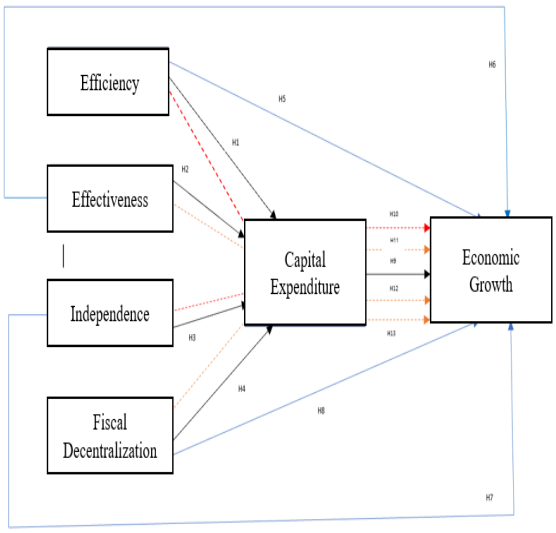


Figure 5. Conceptual Framework

The research hypothesis based on the conceptual framework and problem formulation in this study are as follows:

1. Efficiency has a negative and significant effect on capital expenditure in regencies/cities of Sumatra Utara Province.
2. Effectiveness has a positive and significant effect on capital expenditure in regencies/cities of Sumatra Utara Province.
3. Independence has a positive and significant effect on capital expenditure in regencies/cities of Sumatra Utara Province. Fiscal decentralization has a positive and significant effect on capital expenditure in regencies/cities of Sumatra Utara Province.
4. Efficiency has a negative and significant effect on economic growth in regencies/cities of Sumatra Utara Province.
5. Effectiveness has a positive and significant effect on economic growth in regencies/cities of Sumatra Utara Province.
6. Independence has a positive and significant effect on economic growth in regencies/cities of Sumatra Utara Province.
7. Fiscal decentralization has a positive and significant effect on economic growth in regencies/cities of Sumatra Utara Province.
8. Fiscal decentralization has a positive and significant effect on economic growth in regencies/cities of Sumatra Utara Province.
9. Capital expenditure has a positive and significant effect on economic growth in districts/cities in Sumatra Utara Province.
10. Capital expenditure can significantly mediate the relationship between effectiveness and economic growth in districts/cities in Sumatra Utara Province.
11. Capital expenditure can significantly mediate the relationship between independence and economic growth in districts/cities in Sumatra Utara Province.
12. Capital expenditure can significantly mediate the relationship between fiscal decentralization and economic growth in districts/cities in Sumatra Utara Province.

MATERIALS & METHODS

This study uses data obtained from the Budget Realization Report (LRA) for the 2018-2022 period via the Internet using the official website of the Central Statistics Agency (BPS) of Sumatra Utara Province www.bps.go.id, the official website of Sumatra Utara Province www.sumutprov.go.id, and other sites that support the research. The population in this study consisted of 33 districts/cities throughout Sumatra Utara Province, consisting of 25 district governments and 8 city governments. The sampling method used in this study is the saturated sampling method. Saturated sampling is a sampling technique that uses all members of the population as samples (Sugiyono, 2018). The data analysis technique in this study used the EViews 10 program.

RESULT

A. Descriptive Statistics Results

Descriptive statistics in this study are used to provide information on research variables such as Efficiency Ratio, Effectiveness, Independence, and Fiscal Decentralization in the districts/cities of Sumatra Utara Province for the period 2018-2022.

Table 10. Descriptive Statistics

	Efficiency	Effectiveness	Independence	Fiscal Decentralization	Capital Expenditure	Economic Growth
Mean	98.67	113.73	13.47	8.94	16.98	3.44
Median	99.75	96.86	10.26	7.07	16.2	4.24
Maximum	139.97	647.11	84.83	38.07	42.24	6.05
Minimum	33.06	21.83	1.71	1.06	4.86	-1.98
Std. Dev.	10.12	73.34	12.98	6.24	5.81	2.12
Observation	165	165	165	165	165	165

Source: Results processed with EViews

The efficiency value has a statistical result range of 33.06 - 139.97, with an average value (mean) of 98.67 and a standard deviation value of 10.12. The minimum statistical value of 33.06 was owned by Gunung Sitoli City in 2020. Based on the Decree of the Minister of Home Affairs Number 690,900,327 of 1996, the value of 33.06 is included in the very efficient criteria.

The highest efficiency value (maximum) of 139.97 is owned by North Local Government Revenueang Lawas Regency in 2021 and is included in the inefficient category. The financial performance of a region is said to be increasingly efficient if the results of this ratio measurement are smaller and vice versa. The effectiveness value has a statistical result range of 21.83 - 647.11, with an average value (mean) of 113.73 and a standard deviation value of 73.34. The minimum statistical value of 21.83 is owned by North Nias Regency in 2021. Based on the Minister of Home Affairs Decree number 690,900,327 of 1996, the value of 21.83 is included in the ineffective criteria, and the maximum value of 647.11 with the very effective criteria is owned by Nias Regency in 2022.

The independence value has a statistical result range of 1.71 - 84.83, with an average value (mean) of 13.47 and a standard deviation value of 12.98. The minimum statistical value of 1.71 was owned by South Nias Regency in 2020, and it is included in the Instructional criteria, namely, the role of the central government is more dominant than the independence of the regional government, and the region is unable to implement regional autonomy. The maximum value of 84.83 was owned by Medan City in 2019, entering the Delegative criteria, namely that there is no more central government interference and the region is competent and independent in carrying out regional autonomy affairs.

The fiscal decentralization value has a statistical result range of 1.06 - 38.07 with an average value (mean) of 8.94 and a standard deviation value of 6.24. The minimum statistical value of 1.06 was owned by South Nias Regency in 2020, meaning that South Nias Regency has a very low financial capacity for generating Local Government Revenue compared to the total revenue in its region. However, in 2018, Medan City had the highest efficiency value (maximum) of 38.07, meaning that it has a low criteria financial capacity for generating Local Government Revenue in its region.

The statistical value of capital expenditure allocation ranges from 4.86 - 42.24, with an average value (mean) of 16.98. The quality standards set by the Directorate General of Regional Financial Development of the Ministry of Home Affairs state that for each allocation of capital expenditure in each region, there is a minimum limit of 30%. The average value of 16.98 indicates that the average district/city in Sumatra Utara Province during 2018-2022 has not been able to meet the established standards. The low statistical value of capital expenditure allocation of 4.86 is owned by Simalungun Regency in 2020, while the maximum value of 42.24 is owned by Central Tapanuli Regency in 2022, meaning that in 2022, Central Tapanuli Regency the proportion of capital expenditure to total regional expenditure is above the predetermined standard, which is a minimum of 30%.

The dependent variable in this study, namely economic growth, has an average value (mean) of 3.44 with a minimum value of -1.98 owned by Medan City in 2020. It indicates that in 2020, the growth of Medan City experienced a contraction (minus), meaning that there was no increase in the growth of gross regional domestic product. The maximum value of economic growth of 6.05 was owned by Gunung Sitoli City in 2018. The standard deviation value is 2.12, which is lower than the average value. It indicates that the data distribution is good for the economic growth variable in the observation of this study.

B. Panel Data Regression Model Selection

The Chow test, Hausman test, and Lagrange multiplier test can be used to choose the right model for managing panel data. The models selected for further research are:

1) Substructural Path Analysis I

The analysis used in this study is path analysis with panel data. This technique tests whether the variables of Efficiency, Effectiveness, Independence, and Fiscal Decentralization affect Capital Expenditure.

Selection of Path Analysis with Substructural Panel Data I

Chow Test Substructural I

The Chow test functions to determine whether the common effect or fixed effect model is most appropriate to use in panel data.

Table 11. Chow Test Result

Effects Test	Statistic	d.f.	Prob.
Cross-section F	3.198950	(30,120)	0.0000
Cross-section Chi-square	91.084334	30	0.0000

Source: Results processed with EViews

Based on Table 11, the Cross Section Chi-square value is obtained with a Prob. Value of 0.000 <α (0.05), so the selected estimation model is the fixed effect model.

Hausman Substructural Test I

When the results obtained by the Chow test are a fixed effect model, the next step is to conduct a Hausman test.

Table 12. Hausman Substructural Test I

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	0.220535	4	0.9943

Source: Results processed with EViews

Based on Table 12 from the results of the Hausman test, it is known that the cross-section random value has a probability value of 0.9943 > 0.05, so the estimation model used is the random effect model (REM). According to Gujarati (2005), if the estimation model is already General Least Square, then the classical assumption test of Normality, Heteroscedasticity, Multicollinearity, and Autocorrelation is not needed. Because the nature of the General Least Square estimation model already meets the requirements of the classical assumption test.

Table 13. Random Effect Model Substructural I Test Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
X1_	-0.144845	0.042562	-3.403184	0.0009
X2	0.009291	0.006581	1.411809	0.1601
X3_	-0.190855	0.232333	-0.821472	0.4127
X4_	0.245080	0.409377	0.598666	0.5503
C	30.45368	4.425249	6.881799	0.0000
Effects Specification				
			S.D.	Rho
Cross-section random			3.461190	0.3480
Idiosyncratic random			4.737282	0.6520
Weighted Statistics				
R-squared	0.087848	Mean dependent var		8.866750
Adjusted R-squared	0.063524	S.D. dependent var		4.833251
S.E. of regression	4.677220	Sum squared resid		3281.458
F-statistic	3.611551	Durbin-Watson stat		1.257957
Prob(F-statistic)	0.007677			
Unweighted Statistics				
R-squared	0.079899	Mean dependent var		16.98413
Sum squared resid	4848.584	Durbin-Watson stat		0.851369

Source: Results processed with EViews

Substructural Hypothesis Test I

a) Simultaneous Test (f-statistic test) Substructural I

In Table 13, the number of samples (n) is 155 observation data and the number of parameters (k) is 5, so that df1 = 5 - 1 = 4 is obtained; df2 = n - k = 155 - 5 = 150, then at α = 0.05, Ftable = 2.431 is obtained. Based on Table 4.7, the Fcount value (3.611)> Ftable (2.431) and significance (0.007) <α (0.05). It means that the variables Efficiency, Effectiveness, Independence, and Fiscal Decentralization simultaneously have a significant effect on Capital Expenditure.

b) Partial Test (Statistical t Test) Substructural I

Based on Table 13, the panel data estimation model using REM, the following path analysis equation is obtained:

Z = 30.4530.144 X1 + 0.009 X2 - 0.190 X3 + 0.245 X4

Based on Table 13, it is obtained with (n) = 155, number of parameters (k) = 5, df = (n – k) = 155 – 5 = 150, then at the error level α

= 0.05, the t table = 1.975 is obtained as follows:

- Efficiency has a negative and significant effect on the allocation of Capital Expenditure,
- Effectiveness has a positive and insignificant effect on the allocation of Capital Expenditure,
- Independence has a negative and insignificant effect on the allocation of Capital Expenditure,
- Fiscal Decentralization has a positive and insignificant effect on the allocation of Capital Expenditure.

2) Substructural Path Analysis II

The analysis used is path analysis with panel data. This technique is to test whether the variables Efficiency, Effectiveness, Independence, Fiscal Decentralization, and Capital Expenditure affect Economic Growth.

Selection of Linear Regression Models for Substructural Panel Data II

Chow Test Substructural II

The Chow test functions to determine whether the common effect or fixed effect model is most appropriate to use in panel data.

Table 14. Substructural Chow Test II

Effects Test	Statistic	d.f.	Prob.
Cross-section F	1.197769	(30,119)	0.2449
Cross-section Chi-square	40.899815	30	0.0886

Source: Results processed with EViews

Based on Table 14, the Cross Section Chi-square Prob. The value is 0.088 > α (0.05), so the selected estimation model is the common effect model.

Lagrange Multiplier Test (LM-Test) Substructural II

When the results obtained from the Chow test are the common effect model, the next step is to conduct the LM test.

Table 15. LM Test Substructural II

Null (no rand. effect) Alternative	Cross-section One-sided	Period One-sided	Both
Breusch-Pagan	1.267587 (0.2602)	1109.809 (0.0000)	1111.077 (0.0000)

Source: Results processed with EViews

Based on Table 15, from the results of the LM-test, it is known that both value has a significance value of 0.000 <0.05, so the estimation model used is the Random Effect Model (REM) model. According to Gujarati (2005), if the estimation model is already Generalized Least Square, then the classical assumption test of Normality, Heteroscedasticity, Multicollinearity, and Autocorrelation is not needed because the nature of the Generalized Least Square estimation model already meets the requirements of the classical assumption test.

Table 16. Random Effect Model Substructural II Test Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
X1	0.033248	0.016001	2.077787	0.0394
X2	0.005699	0.002476	2.301398	0.0228
X3	-0.062732	0.076975	-0.814961	0.4164
X4	0.074671	0.128334	0.581851	0.5615
Z	0.136849	0.027060	5.057218	0.0000
C	-2.679194	1.765083	-1.517885	0.1312
Effects Specification				
			S.D.	Rho
Cross-section random			0.000000	0.0000
Idiosyncratic random			1.883888	1.0000
Weighted Statistics				
R-squared	0.196756	Mean dependent var		3.442774
Adjusted R-squared	0.169801	S.D. dependent var		2.108351
S.E. of regression	1.921029	Sum squared resid		549.8627
F-statistic	7.299550	Durbin-Watson stat		2.058083
Prob(F-statistic)	0.000004			
Unweighted Statistics				
R-squared	0.196756	Mean dependent var		3.442774
Sum squared resid	549.8627	Durbin-Watson stat		2.058083

Source: Results processed with EViews

Substructural Hypothesis Test II

a) Simultaneous Test (f-statistic test) Substructural II

In Table 16, the number of samples (n) is 155 observation data, and the number of parameters (k) is 5, so that df1 = 6 - 1 = 5; df2 = n - k = 155 - 6 = 149 is obtained, then at α = 0.05 Ftable = 2.274 is obtained. Based on Table 4.14, the Fcount value (7.299)> Ftable (2.274) and significance (0.00) <α (0.05). It means that the variables of

efficiency, effectiveness, fiscal decentralization, and capital expenditure affect economic growth.

Substructural Direct Effect Test II

Based on Table 16, the panel data estimation model using the REM model, the path analysis equation with panel data is obtained as follows:

Y = -2.679 + 0.033X1 + 0.005X2 - 0.062X3 + 0.074X4 + 0.136Z

Based on Table 16, it is obtained with (n) = 155, number of parameters (k) = 4, df = (n – k) = 155 – 6 = 149, then at the error level α = 0.05, the t table = 1.976 is obtained as follows:

- Efficiency has a positive and significant effect on Economic Growth,
- Effectiveness has a positive and significant effect on Economic Growth
- Independence has a negative and insignificant effect on Economic Growth,
- Fiscal Decentralization has a positive and insignificant effect on Economic Growth,
- Capital Expenditure has a positive and significant effect on Economic Growth,

Indirect Effect Test

The indirect effect test is conducted using the Sobel test, which can be seen as follows:

Table 17. Indirect Effect (Sobel Test)

Interaction	T_{stat}	Probability	Description
relationship between efficiency and economic growth through capital expenditure	-2,834 < 1,96	0,004 < 0,05	Able to mediate significantly
relationship between effectiveness and economic growth through capital expenditure	1,437 < 1,96	0,150 > 0,05	Not able to mediate significantly
relationship between independence and economic growth through capital expenditure	-0,808 < 1,96	0,418 > 0,05	Not able to mediate significantly
the relationship between fiscal decentralization and economic growth through capital expenditure	0,594 < 1,96	0,551 > 0,05	Not able to mediate significantly

Source: Results processed with EViews

CONCLUSION

Based on the research results of the Analysis of the Influence of Regional Financial Performance on Economic Growth with Capital Expenditure Allocation as an Intervening Variable in Regencies/Cities of Sumatra Utara Province, it can be concluded:

1. Efficiency has a negative and significant effect on capital expenditure allocation.
2. Effectiveness has a positive and insignificant effect on capital expenditure allocation.
3. Independence has a negative and insignificant effect on capital expenditure allocation.
4. Fiscal Decentralization has a positive and insignificant effect on capital expenditure allocation.
5. Efficiency has a positive and significant effect on Economic Growth.
6. Effectiveness has a positive and significant effect on Economic Growth.
7. Independence has a negative and insignificant effect on Economic Growth.
8. Fiscal Decentralization has a positive and insignificant effect on Economic Growth.
9. Capital expenditure allocation has a positive and significant effect on economic growth.
10. Capital expenditure allocation can mediate the relationship between efficiency and economic growth significantly.
11. Capital expenditure allocation is unable to mediate the relationship between effectiveness and economic growth.
12. Capital expenditure allocation is unable to mediate the relationship between independence and economic growth.

13. Capital expenditure allocation is unable to mediate the relationship between fiscal decentralization and economic growth.

SUGGESTIONS

Based on the results of the research conducted, several suggestions can be given by the researcher, including:

1. For district/city governments

a) Efforts are made so that each district/city can manage and increase its Regional Original Income (Local Government Revenue) so that it increases its Regional Income. Some ways to increase Local Government Revenue include: Optimizing the management of natural resources. Regional governments can increase their regional income by optimizing the management of natural resources, such as agricultural products, plantations, and fisheries.

b) Developing local potential or MSMEs, which include financial support, training, and product marketing.

c) Improving the quality and quantity of infrastructure so that it can increase accessibility and develop the economy through transportation.

d) Improving financial management efficiency by increasing the efficiency of regional financial management, such as reducing operational costs and increasing regional income.

2. In increase the allocation of the Local Government Budget and its management for program activities that can be directly felt by the community, such as infrastructure development and other public services.

3. The allocation of capital expenditures must be increased to 30% of the Local Government Budget because, in addition to increasing regional investment, it can also grow economic activity in the region.

2. For further research

a) Further research can be conducted by adding or changing other variables that are not yet included in this study.

b) Variables that do not influence economic growth should be reviewed for further research.

c) Further researchers should add intervening variables that are considered capable of mediating the relationship between independent variables and dependent variables.

Declaration by Authors

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