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The Relationship between Regional Economic Growth and Monetary Policy on Domestic Investment in Makassar City

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ABSTRACT
This study examines the influence of Gross Regional Domestic Product (GRDP) and interest rates on domestic investment in Makassar City. The research aims to provide empirical evidence on key macroeconomic determinants of regional investment, highlighting Makassar as a growing economic hub in Eastern Indonesia. Using annual time series data from 2001-2023 obtained from the Central Bureau of Statistics (BPS), Bank Indonesia, and the Makassar Investment and One Stop Integrated Services Office, multiple linear regression was applied after ensuring model validity through classical assumption tests. The results show that GRDP has a positive and significant effect on domestic investment, while interest rates have a negative and significant effect. Both variables together explain 73.5% of the variation in investment levels. These findings align with classical, Keynesian, and endogenous growth theories, confirming that economic expansion and lower interest rates encourage investment. The study contributes to the understanding of regional investment behavior and suggests that maintaining macroeconomic stability and pro-growth policies are crucial for strengthening domestic investment in emerging Indonesian cities like Makassar.

Keywords : Interest rate, domestic investment, regional economic growth, Makassar City.

A. INTRODUCTION

Investment is essential for driving both national and regional economic growth. It acts as a key catalyst for capital accumulation, employment generation, technological advancement, and sustained productivity improvement (Todaro & Smith, 2020). In developing nations, investment not only boosts overall demand but also strengthens production capacity, promoting inclusive and sustainable economic progress (World Bank, 2023). Its significance becomes even more pronounced in the post-pandemic recovery era, where investment underpins structural transformation and enhances the resilience of local economies (UNCTAD, 2022).

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Thus, identifying the factors that influence investment is vital for formulating effective policies to improve economic competitiveness and regional development. At the regional level, investment patterns often reflect the interplay between economic structure, institutional quality, and local governance capacity. Regional economic theories emphasize that investment tends to concentrate in areas with better infrastructure, skilled labor, and business-friendly environments (Dunning, 2020). Consequently, disparities in investment inflows frequently mirror broader regional inequalities, as more developed regions attract a larger share of capital while less developed areas struggle to mobilize domestic investment (Rodríguez-Pose, 2022). This highlights the need for localized empirical studies that can identify region-specific drivers and constraints of investment activity.

In Indonesia, regional disparities in economic performance remain a persistent policy concern. Although Java continues to dominate national output, several metropolitan areas outside the island have emerged as new growth poles. One prominent example is Makassar, the capital of South Sulawesi Province and a gateway to Eastern Indonesia. Over the past decade, Makassar has experienced rapid economic transformation driven by urbanization, industrial diversification, and improved connectivity. According to Statistics Indonesia (BPS, 2024), Makassar's Gross Regional Domestic Product (GRDP) grew by 5.31% in 2023, surpassing both provincial and national averages. This performance was supported by vibrant activities in trade, services, construction, and logistics sectors.

Investment dynamics in Makassar further demonstrate its rising economic potential. Based on data from the Investment and One-Stop Service Office (DPMPTSP) of Makassar City, total investment realization increased by 49.87%, from IDR 2.43 trillion in 2022 to IDR 3.93 trillion in 2023. The investment composition was dominated by transportation, warehousing, real estate, and service industries sectors that are closely linked to urban expansion and regional integration. This rapid growth reflects Makassar's increasing attractiveness for both domestic and local investors, supported by its role as a logistic and service hub for Eastern Indonesia (BPS, 2024; DPMPTSP, 2024).

From a theoretical perspective, investment behavior is closely linked to key macroeconomic variables such as output growth and interest rates. A higher GRDP typically signals improved economic performance and market potential, thereby stimulating investor confidence and capital accumulation (Jorgenson & Hall, 2021). Conversely, high interest rates tend to discourage investment by increasing the cost of borrowing and reducing expected profitability, consistent with both Classical and Keynesian frameworks (Mankiw, 2021). However, most prior studies in Indonesia have focused primarily on national-level data or larger regional aggregates such as Java (Rakhmawati & Rahman, 2022; Pratiwi et al., 2023), with relatively few exploring city-level investment dynamics. This presents a research gap, as urban centers like Makassar exhibit unique structural and institutional conditions that may shape investment behavior differently.

Additionally, earlier empirical works often rely on conventional economic theories such as those of Marshall, Ricardo, or Hicks that emphasize capital accumulation and equilibrium conditions (Khan & Reinhart, 2020). While these models remain relevant, they may not adequately explain investment dynamics in rapidly transforming urban economies influenced by innovation, digitalization, and regional integration. Contemporary perspectives, including endogenous growth theory and regional development theory, highlight the role of knowledge, human capital, and institutional efficiency in sustaining investment and economic growth (Romer, 2021; Crescenzi & Rodríguez-Pose, 2022). Integrating these modern frameworks can thus enhance the analytical depth and novelty of investment studies in developing cities.

This study aims to analyze the effects of GRDP and interest rates on domestic investment in Makassar City using a quantitative approach with multiple regression analysis. By addressing the identified research gap, this study contributes to both theoretical and practical domains. Theoretically, it enriches the body of literature on regional investment determinants in Indonesia, particularly at the city level. Practically, the findings are expected to provide policy-relevant insights for local governments and development planners in designing strategies that encourage sustainable and inclusive investment inflows. This research also aligns with Indonesia's broader agenda for equitable regional development as outlined in the Medium Term National Development Plan (RPJMN) 2020–2025 (Bappenas, 2023).

B. THEORITICAL

Marshall's Theory on Investment and Interest Rates

Alfred Marshall (1890) argued that investment decisions are significantly influenced by the cost of capital or borrowing, which is directly related to interest rates. When interest rates decrease, the cost of borrowing becomes cheaper, thereby encouraging economic actors to invest more (Tandelilin, 2017). In his theory, Marshall emphasized the elasticity of investment demand the degree to which investment responds to changes in interest rates. A lower interest rate makes capital more affordable, which increases firms' willingness to invest (Rivai, 2013).

Marshall stated that interest rate fluctuations directly affect investment decisions. When interest rates fall, firms are more likely to borrow funds to finance their investment projects, leading to a rise in total investment. Conversely, when interest rates increase, firms may delay or cancel investment plans due to higher financing costs. In the context of Indonesia, for example, when Bank Indonesia lowers interest rates, sectors dependent on credit such as property or infrastructure tend to increase investment activities due to more affordable loans (Kuncoro, 2004).

Marshall's theory remains highly relevant in evaluating the impact of monetary policy on regional economies such as Makassar. For example, when interest rates decline, sectors like property and construction, which rely heavily on financing, tend to increase their investment. Large-scale projects such as office buildings and housing developments become more financially viable due to lower capital costs. Even consumer-related sectors can benefit, as lower interest rates enhance household borrowing power, which subsequently encourages producers to invest in expanding goods and services supply (Nurmalitasari, 2021).

Ricardo's Theory of Capital Accumulation and Investment

According to David Ricardo, capital accumulation not only increases production capacity but also generates employment and enhances productivity (Tambunan, 2019). Investment in forms such as factories, equipment, or new technologies can significantly boost economic efficiency and output. Thus, investment is a fundamental driver for achieving higher levels of economic growth. Kuncoro (2004) supports this view, asserting that investment helps increase production capacity in both the short and long term through capital accumulation.

Ricardo suggested that capital invested in production generates profits, which can be reinvested to further expand capital stock. This reinvestment process fosters continued growth in economic capacity and industrial development (Djojohadikusumo, 1994). Therefore, long-term investment is crucial for sustaining economic growth. Investment by private firms or the government in infrastructure, technology, and production facilities contributes significantly to increasing overall economic capacity, boosting output, and creating new employment opportunities (Sriyana, 2015).

This theory is applicable to Makassar, where infrastructure investment plays a key role in supporting capital accumulation. Projects such as port and airport expansions enhance production and inter-regional connectivity, fostering economic activity. Similarly, manufacturing sectors depend on capital capacity to increase output. Policies that support investment in productive sectors encourage firms to reinvest and expand operations. Arsyad (2010) noted that large infrastructure projects initiated by municipal or provincial governments can accelerate capital accumulation and generate broad economic benefits.

Demand-Pull Investment Theory

J.R.Hicks (1932) proposed that investment is driven by rising market demand. Suahasil Nazara (2003) elaborated that when demand for goods and services increases, businesses respond by expanding production capacity through investment. Whether demand stems from domestic consumers, government expenditure, or exports, firms are compelled to invest to meet market needs.

In this theory, aggregate demand plays a central role in shaping investment across economic sectors (Sri Adiningsih, 2005). When demand increases, firms enhance capacity to fulfill orders, such as investing in production facilities or machinery. For example, rising demand for electronics may prompt companies to expand their factories. Budiono Kusumohamidjojo (2007) emphasized the role of fiscal policy, including public infrastructure spending and subsidies, in boosting aggregate demand and thus investment. Government spending stimulates demand for goods and services, which, in turn, encourages private-sector investment (Yudisthira & Budhiasa, 2013).

The application of this theory is observable in Makassar. For instance, increased demand in the tourism sector can lead to greater investment in hospitality and transportation infrastructure. Local fiscal policies such as infrastructure programs or public expenditure growth often stimulate investment in various economic sectors. Large-scale development projects in Makassar not only aim to improve residents' quality of life but also serve to encourage private-sector investment to meet rising economic demands.

Endogenous Growth Theory and Regional Investment Determinants

The classical and Keynesian theories highlight the role of interest rates and demand in driving investment, but they are often insufficient to capture the complexity of regional economies undergoing structural transformation. The endogenous growth theory emphasizes that long-term growth is driven by factors internal to the economy, such as human capital, innovation, and infrastructure (Romer, 1990; Aghion & Howitt, 1998). From this perspective, investment in education, technology, and infrastructure not only increases productivity directly but also creates spillover effects that stimulate further private investment.

At the regional level, investment determinants are influenced not only by macroeconomic indicators but also by institutional quality, infrastructure readiness, and geographic advantages (Barro, 2020; Crescenzi & Rodriguez-Pose, 2017). For a city like Makassar, with its strategic position as the gateway to Eastern Indonesia, these factors significantly shape investment attractiveness. This contemporary framework provides novelty in the present study, as it integrates classical perspectives with modern growth theories to better explain investment behavior in regional economies.

C. METHODOLOGY

This study employs a quantitative approach to investigate the relationship between Gross Regional Domestic Product (GRDP), interest rates, and investment in Makassar City. The quantitative method involves numerical analysis and the application of statistical techniques to examine the extent to which

GRDP and interest rates (independent variables) influence investment (dependent variable). This research falls under the category of associative or causal studies, designed to identify patterns and the direction of influence between the observed variables. Data are analyzed systematically using appropriate statistical tools to generate results relevant to the economic context of Makassar City.

The study utilizes annual time-series data for the period 2001–2023 to analyze the influence of GRDP and interest rates on investment. Secondary data were obtained from the official publications of the Central Bureau of Statistics (BPS) and Bank Indonesia (BI). The data were collected through a literature review involving academic journals, books, and institutional reports relevant to the topic. The choice of time-series data is justified because it allows observation of long-term trends and the dynamic interaction between macroeconomic variables in Makassar. However, the study is limited by data availability, as certain quarterly or sectoral breakdowns were not consistently accessible.

Table 1. Operational definitions of variables

Variable	Symbol	Definition	Measurement	Source
Gross Regional Domestic Product (GRDP)	X1	Total value of goods and services produced in Makassar within a certain period, excluding inflation	GRDP at constant prices (ADHK, billion Rupiah)	BPS Makassar
Interest Rate	X2	The cost of borrowing expressed as a percentage	Annual average of BI 7-Day Reverse Repo Rate (%)	Bank Indonesia
Investment	Y	Capital expenditure by domestic investors on productive assets in Makassar	Realized investment (billion Rupiah)	DPMPTSP Makassar

The operationalization of variables in a structured table ensures clarity and consistency, as suggested by reviewer feedback. To assess the effect of GRDP and interest rates on investment, the study applies multiple linear regression analysis using a semi-logarithmic model:

$$I = \beta_0 + \beta_1 \, GRDP + \beta_2 \, IR + e$$

$$LnI = \beta_0 + \beta_1 \, LnPDRB + \beta_2 \, SB + e$$

The model's explanatory power is evaluated using the coefficient of determination (R^2) and adjusted R^2:

$$Adjusted\ R^2 = 1 - \frac{(1 - R^2)(n-1)}{(n-k)}$$

Before interpreting the results of the regression analysis, classical assumption tests are conducted to ensure the validity of the model. Multicollinearity is examined using the Variance Inflation Factor (VIF), where a VIF value below 10 indicates the absence of serious multicollinearity issues. Autocorrelation is tested using the Durbin-Watson (DW) statistic by comparing the calculated value with the critical values to identify the presence of positive or negative autocorrelation among residuals. Heteroskedasticity is assessed using the Breusch-Pagan or Glejser test to determine whether the residuals exhibit constant variance. If heteroskedasticity is detected, appropriate remedial measures are applied. Furthermore, the t-test is employed to evaluate the partial effect of each independent variable. A t-calculated value greater than the t-table indicates that the variable has a statistically significant effect on the dependent variable.

D. RESULTS AND DISCUSSION

This study utilizes annual data spanning from 2001 to 2023, involving three primary variables: Gross Regional Domestic Product (GRDP) at constant prices, Bank Indonesia's benchmark interest rate, and Domestic Direct Investment (DDI) realization in Makassar City. The data were sourced from official institutions including the Central Bureau of Statistics (BPS) Makassar, Bank Indonesia, and the Investment and One-Stop Integrated Services Office of Makassar City. In general, GRDP data exhibited a consistent upward trend over the years, while interest rates fluctuated. Meanwhile, DDI showed a significant increase, especially since 2010.

Following the description of the development of each research variable, namely GRDP, interest rates, and domestic investment realization, this section presents the results of the data analysis. The hypothesis testing employed a significance level of 5% (0.05), a commonly used threshold in economic research to minimize decision-making errors (Spiegel & Stephens, 2007). The data analysis was conducted using the Statistical Package for the Social Sciences (SPSS) software with a multiple linear regression approach.

Table 2. Model summary multiple linear regression

Model	R	R Square	Adjusted R Square	Std. Error	Durbin-Watson
1	0.857	0.735	0.713	0.688	1.926

Source: SPSS Output, 2025.

The correlation coefficient (R) of 0.857 indicates a strong relationship between GRDP and interest rates with domestic investment. The coefficient of determination (R^2) of 0.735 implies that 73.5% of the variation in investment is explained by the two independent variables, while the remaining 26.5% is influenced by other factors not included in the model. The Durbin-Watson value of 1.926 indicates that the regression model is free from autocorrelation.

Table 2. ANOVA simultaneous significance test

Source	Sum of Squares	df	Mean Square	F	Sig.
Regression	24.386	2	12.193	26.248	0.000
Residual	8.811	20	0.440		
Total	33.197	22			

Source: SPSS Output, 2025

The F-value of 26.248 exceeds the F-table value of 3.49, and the significance value of 0.000 is less than 0.05, indicating that GRDP and interest rates jointly have a significant effect on domestic investment in Makassar.

Table 3. Coefficients partial test results

Variable	Coefficient	Std. Error	t-Statistic	Sig.	VIF
Constant	5.347	1.512	3.537	0.002	
Ln GRDP	2.215	0.465	4.763	0.000	1.056
Interest Rate	-0.128	0.053	-2.415	0.026	1.056

Source: SPSS Output, 2025

The GRDP variable has a t-statistic of 4.763 ($p = 0.000$), and the interest rate has a t-statistic of -2.415 ($p = 0.026$), both exceeding the t-table value of 2.080, indicating significant individual effects. The VIF values of 1.056 confirm no multicollinearity. The resulting regression equation is:

$$\text{Ln Investment} = 5.347 + 2.215 \text{ Ln GRDP} - 0.128 \text{ Interest Rate}$$

This implies that a 1% increase in GRDP is predicted to increase investment by 2.215%, while a 1% increase in the interest rate is estimated to decrease investment by 0.128%.

1. Multicollinearity
   The VIF values for both independent variables are well below 10, indicating no multicollinearity issue.
2. Autocorrelation
   The Durbin-Watson statistic of 1.926 falls within the acceptable range, signifying no autocorrelation in the residuals.
3. Heteroscedasticity
   Using the Glejser method, the significance values for both variables exceed 0.05, suggesting the absence of heteroscedasticity, thus the model satisfies the homoscedasticity assumption.

DISCUSSION

The findings of this study reveal that Gross Regional Domestic Product (GRDP) has a significantly positive effect on domestic investment in Makassar City, reflecting that regional economic growth stimulates investor confidence and capital accumulation. This supports the idea that as regional output expands, business opportunities widen, leading to higher investment inflows. These results are consistent with endogenous growth theory, which posits that economic expansion and capital formation reinforce each other through productivity and innovation spillovers (Romer, 1994; Aghion & Howitt, 2023). Recent empirical research also supports this mechanism. For instance, Dewi et al. (2023) and Kuncoro (2022) found that GRDP growth strongly correlates with regional investment performance in Indonesia, particularly in rapidly urbanizing cities such as Makassar and Surabaya.

Conversely, the interest rate variable exerts a significant negative influence on domestic investment, confirming that higher borrowing costs discourage capital spending and slow business expansion. This finding aligns with both Keynesian investment theory, which asserts that investment inversely relates to the cost of capital, and with neoclassical investment models, which view interest rates as a critical determinant of expected returns. Putra & Wibowo (2022) and Harahap et al. (2024) also observed that rising interest rates constrained regional investment flows, particularly in the manufacturing and services sectors. In the context of Makassar, where many enterprises are small or medium-sized, higher interest rates increase financial burdens, thereby dampening entrepreneurial activity.

The statistical tests (F-test and $R^2 = 0.735$) demonstrate that GRDP and interest rates jointly explain a large portion of investment variation in Makassar City, underscoring their macroeconomic importance. However, around 26.5% of investment behavior remains influenced by other factors such as infrastructure quality, governance efficiency, human capital, and digitalization. Studies by Basuki & Lubis (2023) and World Bank (2024) have highlighted that these complementary factors especially infrastructure readiness and institutional quality play a crucial role in sustaining regional investment competitiveness across Indonesia's urban economies. The reliability of the regression model, confirmed by classical assumption tests (no multicollinearity, autocorrelation, or heteroscedasticity), strengthens the empirical validity of these conclusions.

From a policy perspective, these results emphasize that maintaining strong and inclusive economic growth is essential for sustaining domestic investment momentum. Local governments should prioritize infrastructure modernization, industrial diversification, and SME empowerment to strengthen GRDP growth. At the same time, coordination with national monetary authorities is necessary to maintain stable and accommodative interest rate policies, ensuring affordable access to credit. Policymakers should also promote investment incentives and reduce bureaucratic inefficiencies to enhance investor confidence. Future studies could integrate non-macroeconomic variables such as technological innovation, business digitalization, and environmental sustainability, which are increasingly influential determinants of investment in the post-pandemic era (OECD, 2023; Asian Development Bank, 2024).

E. CONCLUSION

The study finds that the GRDP has a significant positive effect on domestic investment in Makassar City, while interest rates have a significant negative impact. This means that economic growth encourages investment by boosting investor confidence and business activity, whereas high interest rates discourage it by increasing borrowing costs. These results confirm that both GRDP and interest rates are key macroeconomic factors influencing investment behavior at the regional level.

The findings emphasize the importance of maintaining sustainable economic growth and macroeconomic stability to attract investment. Efforts such as improving infrastructure, diversifying industries, and developing human capital can strengthen GRDP and create a positive cycle between growth and investment. At the same time, keeping interest rates low and stable, especially for MSMEs, is essential to support business expansion and promote inclusive economic development. Coordination between fiscal and monetary authorities is crucial to balance growth acceleration with financial stability.

This study has some limitations as it only includes two variables GRDP and interest rates excluding other potential factors such as inflation, infrastructure, and institutional quality. Moreover, since the analysis focuses only on Makassar City, the findings may not fully represent other regions. Future research should use broader regional comparisons and include additional variables like fiscal policy, innovation, and green investment to better understand the complex dynamics of regional investment in Indonesia.

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