A COMPARATIVE ANALYSIS OF THE EFFECTS OF INVESTMENT AND INFLATION ON ECONOMIC GROWTH

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Abstract

This study aims to analyze and compare the effects of investment and inflation on Indonesia's economic growth from 2023 to 2025. Employing a qualitative descriptive approach and a literature review method, the study draws on secondary data obtained from Statistics Indonesia (BPS) and various scholarly sources. The findings indicate that although inflation in Indonesia remained relatively under control during the period, the declining investment trend contributed significantly to the slowdown in economic growth. Investment was found to have a more dominant role than inflation in promoting economic growth by increasing production capacity, creating employment opportunities, and strengthening the economic structure. Therefore, policies that promote a conducive and sustainable investment climate are required while maintaining price stability. This study provides important implications for macroeconomic policymaking, particularly policies aimed at optimizing the role of investment in Indonesia's national development.

Key words: *Investment, Inflation, Economi Growth*

Introduction

According to Law No. 25 of 2004 concerning the National Development Planning System, Indonesia's economic development aims to improve public welfare sustainably. Meanwhile, Law

No. 17 of 2003 concerning State Finance stipulates that state finances must be managed transparently, efficiently, accountably, and responsibly to promote public welfare and maintain macroeconomic stability. Qurayshilhady (2024) states that economic growth can be measured by changes in a country's real gross domestic product (GDP), which reflect increases or decreases in average income and aggregate production levels. Therefore, GDP serves as an essential indicator for assessing national economic performance and its relationship with other macroeconomic issues. Ardiansyah (2017) further explains that economic growth reflects a country's economic development and progress.

Table 1. Statistics Indonesia (BPS) Data on Economic Growth, 2023–2025

No	Year	GDP
1.	2023	5,05%
2.	2024	5,03%
3.	2025	4,87%

Source: Statistics Indonesia (BPS), 2023–2025.

Based on data from Statistics Indonesia (BPS), Indonesia's economic growth rate declined between 2023 and 2025. The economy grew by 5.05% in 2023, before decreasing to 5.03% in 2024 and further declining to 4.87% in 2025. This slowdown can be attributed to several factors, one of which is weakening household consumption. The decline in purchasing power and reduced expenditure on non-essential goods, such as clothing and footwear, indicate that inflationary pressures and economic uncertainty have encouraged households to adopt more cautious spending behavior. In addition to consumption, investment is another important concern. When economic growth weakens, investors tend to become more cautious about committing capital, particularly amid global uncertainties such as geopolitical tensions, commodity price fluctuations, and high interest-rate policies in advanced economies, which can affect capital flows into Indonesia. As a developing country, Indonesia continues to promote economic growth to improve public welfare.

However, it continues to face several challenges, including fluctuations in investment and inflation. Low investment can slow economic growth by limiting production capacity and job creation. Meanwhile, high inflation reduces purchasing power and household consumption, ultimately hindering economic growth. nvestment can promote economic growth. As investment increases, capital formation also rises, creating new employment opportunities, expanding production capacity, and stimulating economic activity. Haque (2016) states that the pace of economic development can be assessed through the level of investment. Foreign investment also contributes significantly to economic growth in developing countries by influencing employment, production, prices, income, and public welfare. Foreign investment supports the acceleration of economic growth and capital mobilization. The government has focused on increasing investment through pro-industry policies to strengthen the foundations of the national economy. Mutholifa (2019) states that investment is a major driver of economic activity because it can increase output, create employment opportunities, and reduce unemployment. Therefore, formulating a legal and regulatory framework that encourages investment is essential to support the public and private sectors and society as a whole.

Table 2. Statistics Indonesia (BPS) Data on Investment, 2023–2025

No	Tahun	Persentase
1.	2023	4,40%
2.	2024	3,78%
3.	2025	2,12%

Source: Statistics Indonesia (BPS), 2023–2025.

Based on the investment data presented in Table 2, the investment rate exhibited a declining trend over the three-year period. In 2023, it reached its highest level at 4.40%, reflecting relatively stable economic conditions and a supportive investment climate. However, it decreased to 3.78% in 2024. This decline may be associated with several factors, including global economic uncertainty, changes in fiscal and monetary policies, and regulatory barriers that weakened investor interest.

The downward trend continued in 2025, when the investment rate fell sharply to 2.12%. This consistent decline highlights the need to evaluate national investment policies to maintain Indonesia's attractiveness to both domestic and foreign investors. If not addressed promptly, declining investment may slow national economic growth, limit job creation, and increase unemployment. Based on the investment data presented in Table 2, the investment rate exhibited a declining trend over the three-year period. In 2023, it reached its highest level at 4.40%, reflecting relatively stable economic conditions and a supportive investment climate. However, it decreased to 3.78% in 2024. This decline may be associated with several factors, including global economic uncertainty, changes in fiscal and monetary policies, and regulatory barriers that weakened investor interest. The downward trend continued in 2025, when the investment rate fell sharply to 2.12%. This consistent decline highlights the need to evaluate national investment policies to maintain Indonesia's attractiveness to both domestic and foreign investors. If not addressed promptly, declining investment may slow national economic growth, limit job creation, and increase unemployment. Inflation is also an important issue in the context of economic growth. In economics, inflation is regarded as a monetary phenomenon in which changes in the inflation rate can lead to economic instability. According to Keynesian theory, inflation occurs when aggregate demand exceeds aggregate supply because people attempt to consume beyond the economy's productive capacity. In the short term, limited production capacity makes it difficult to increase supply, thereby driving inflation. This condition encourages people to spend money more quickly, thereby increasing the velocity of money. According to Sukirno, as cited in Kalsum (2017), inflation refers to a process of increasing prices viewed within a socioeconomic context. Inflation can also be defined as a continuous upward trend in the prices of goods and services, resulting in a decline in the value of money and reducing its purchasing power relative to those goods and services (BPS, 2021). In developing countries, inflation is often driven not only by monetary factors but also by structural problems, commonly referred to as *cost-push inflation*. This occurs because their economic structures still rely heavily on the agricultural sector. Structural bottlenecks—such as an inelastic food supply, limited foreign exchange reserves due to export values being lower than import values, and constraints on government spending—are among the main causes of this type of inflation.

Figure 1. Indonesia's Inflation Rate, 2023–2025

According to data presented in the BPS graph, Indonesia's inflation rate showed a significant downward trend. Inflation stood at 2.61% in 2023, declined to 1.57% in 2024, and increased slightly to 1.60% in 2025. This trend reflects the government's success in maintaining price stability, despite a slight increase in 2025. Price stability is essential for maintaining investor confidence and ensuring a balance between aggregate demand and aggregate supply.

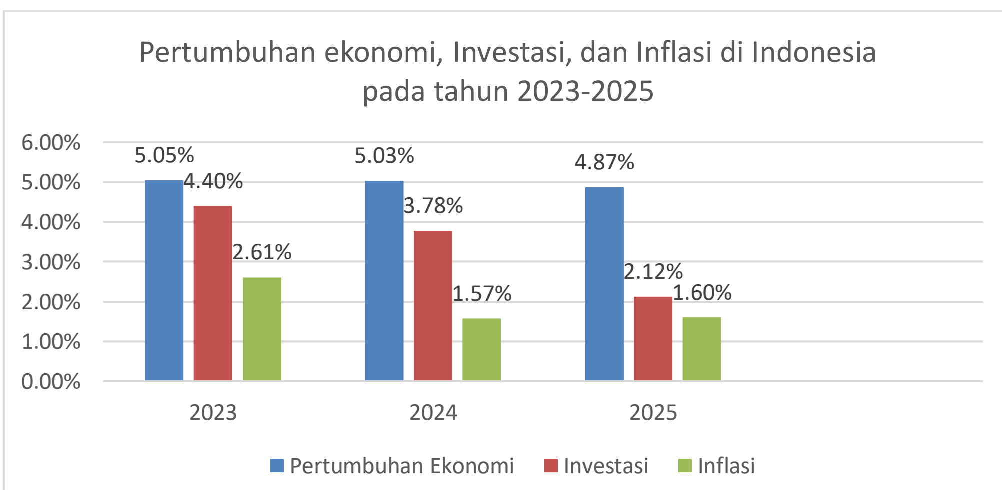

Figure 2. Economic Growth, Investment, and Inflation in Indonesia, 2023–2025

The graph above presents a comparison of Indonesia's economic growth, investment, and inflation from 2023 to 2025. In 2023, Indonesia's economic growth was recorded at 5.05%, accompanied by an investment rate of 4.40% and an inflation rate of 2.61%. These figures indicate that economic growth remained relatively strong and was supported by robust investment, despite moderate inflationary pressures. Meanwhile, Indonesia's economic growth declined further to 4.87% in 2025, accompanied by a sharp decrease in the investment rate to 2.12%, while inflation increased slightly to 1.60%. These data indicate that although inflation remained low and relatively under control, declining investment may have constrained economic growth. This phenomenon supports the assumption of a strong and significant correlation between investment and economic growth. Lower investment tends to reduce productivity and production capacity, which may ultimately slow economic growth. Overall, the graph indicates that controlled inflation alone is insufficient to maintain high economic growth. Investment plays a crucial role in promoting sustainable economic growth. Therefore, future economic policies should place particular emphasis on increasing both domestic and foreign investment while maintaining price stability to ensure a conducive business climate. The discussion above is supported by previous research examining economic growth, investment, and inflation. According to Nujum (2019), investment and inflation affect economic growth, although their effects are not statistically significant.

Method

This study employs a qualitative descriptive approach supported by a literature review to identify the relationship between Indonesia's economic growth and the variables of investment and inflation. The data were obtained from reliable academic and institutional sources, including Bank Indonesia, Statistics Indonesia (BPS), and relevant government ministries. The qualitative descriptive approach was selected because it enables a comprehensive explanation of economic phenomena, particularly the relationships among inflation, investment, and economic growth. As explained by Sanjaya (2015), this method provides an in-depth description of the relationships among variables based on the available data. Meanwhile, according to Putri (2020), a literature review is a data-collection technique involving the examination of various references, including journal articles, books, research reports, and other scholarly documents. In this study, the selected literature focuses on inflation, investment, and economic growth in accordance with the research scope. The literature was reviewed systematically to identify research gaps, strengthen the theoretical framework, and establish a foundation for the analysis. In processing the data, a thematic analysis method was employed by identifying the main themes emerging from the collected literature. The analysis aimed to evaluate patterns of relationships and compare the effects of investment and inflation on economic growth.

Results and Discussion

Economic growth is an important indicator for assessing a country's economic performance. Within a macroeconomic framework, economic growth reflects an increase in production capacity over time, as measured by Gross Domestic Product (GDP). Two important factors that significantly influence economic growth are investment and inflation. Investment contributes to the supply side of the economy, whereas inflation primarily affects the demand side. Investment, whether domestic or foreign, plays a vital role in expanding production capacity and creating employment opportunities. Simangunsong and Barika (2025) argue that increased investment can stimulate the real sector and accelerate economic growth. Similarly, Manullang (2024) emphasizes that investment also contributes to strengthening the long-term economic structure through technological adoption. Large-scale investment has the potential to increase production capacity and generate higher output levels. However, investment may not contribute effectively to employment creation when it is concentrated more heavily in capital-intensive sectors that rely on machinery and technology than in labor-intensive sectors. Consequently, this may lead to higher unemployment (Sutama et al., 2021). The Harrod–Domar growth theory states that investment plays a crucial role in generating sustainable economic growth. The amount of funds available for investment is positively correlated with the ratio of savings to GDP. However, the Solow Growth Model emphasizes that investment in physical capital must be complemented by improvements in labor quality, or human capital, to prevent diminishing marginal returns and sustain long-term economic growth. Investment in the infrastructure sector is an effective form of government intervention. Yahya (2020) found that infrastructure, including roads, ports, and electricity, is positively correlated with economic growth, particularly on the island of Java. A study conducted by Fajar (2024) in Enrekang showed that road and irrigation development can increase agricultural productivity and generate multiplier effects in surrounding areas. However, Surya (2024) emphasized that regional disparities in infrastructure remain a concern, highlighting the need for a more equitable distribution of investment. Human resources (HR) also play an important role. Endogenous growth theory states that improving human capital through education and training contributes to long-term economic growth. Wardani (2024) demonstrated that investment in the education sector has a positive impact on labor productivity and national output. This finding is supported by Akbar et al. (2021), who showed that strengthening the quality of human resources can improve economic efficiency in South Sumatra. In addition to investment, inflation is an important variable that must be managed carefully. Low and stable inflation creates price certainty, preserves people's purchasing power, and provides positive signals to investors. Based on data from Statistics Indonesia (BPS), Indonesia's inflation rate during 2023–2025 ranged from 1.57% to 2.61%, indicating that monetary policy successfully maintained price stability. However, low inflation may also indicate weak domestic demand, which can hinder economic growth (Situmorang & Siregar, 2021). The classical quantity theory of money states that inflation occurs when the money supply increases more rapidly than output growth. However, from a Keynesian perspective, inflation is also influenced by demand-side and cost-side pressures, commonly referred to as *demand-pull inflation* and *cost-push inflation*. In Indonesia, inflation tends to be structural, stemming from supply constraints and inefficiencies in the distribution of goods. When inflation declines, consumers retain greater purchasing power and have more flexibility to adjust their consumption to meet their needs, thereby supporting improved economic performance. Businesses may also be encouraged to increase investment, expand production, and promote economic growth as inflation and interest rates decline. However, high levels of consumer spending can exert upward pressure on inflation. Ultimately, uncontrolled inflation may disrupt economic stability, weaken competitiveness, and reduce people's real income (Fuad, 2018). Several studies have shown that inflation negatively affects economic growth when it exceeds a certain threshold. For example, Saputro (2022) found that inflation above 5% begins to suppress household consumption and reduce private-sector investment. Conversely, inflation maintained within the central bank's target range may stimulate economic activity. A comparison of the effects of investment and inflation on economic growth indicates that investment makes a stronger and more sustainable contribution. Arafah (2024) found that the elasticity of GDP with respect to investment is higher than its elasticity with respect to inflation. This means that a small change in the investment rate has a greater effect on economic growth than fluctuations in inflation. Fitriani (2023) also reported that investment has a positive and significant long-term effect on economic growth, whereas inflation has only a short-term effect. Therefore, in formulating economic development strategies, the government should prioritize the creation of a conducive investment climate while maintaining macroeconomic stability. Thus, both investment and inflation are important and interrelated variables within the economic growth framework. However, based on empirical findings and economic theory, investment appears to be the more significant driver of Indonesia's economic growth. Consequently, the government should continue to strengthen the investment sector, expand infrastructure development, and maintain inflation stability through coordinated fiscal and monetary policies.

Conclusion

Investment plays a more dominant role than inflation. Although inflation remained under control, ranging from 1.57% to 2.61%, the significant decline in investment from 4.40% to 2.12% coincided with a decrease in economic growth from 5.05% to 4.87%. These findings are consistent with the Harrod–Domar theory and the Solow Growth Model. Investment in the real and infrastructure sectors increases production capacity and employment; however, its effectiveness depends on appropriate allocation and human capital development. Inflation tends to have a short-term impact, whereas investment contributes to long-term economic growth. Therefore, improving the investment climate through policies that attract domestic and foreign investment, ensuring equitable infrastructure development, strengthening human capital, and implementing coordinated fiscal and monetary policies are recommended. Further research is needed to examine additional factors influencing economic growth and optimize policy strategies to maximize investment's contribution to sustainable and inclusive economic growth. Overall, Indonesia's economic growth depends on strong and well-directed investment, with inflation control serving as a key element of macroeconomic stability.

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