

Chapter 1

INTRODUCTION

This chapter consists of background of problems, research problems, research objectives, research advantages, hypothesis and systematic writing. In the part of background the writer describes about a reason why take this title. In the part of research problem it describes the problems that will be analyzed. In the part of research objectives it describes the objectives of this research conducted and then in the part of research advantages describe for whom this research results. The next in the part of the hypothesis it describes the any expected of the research that will be examined. As well as in the part of systematic writing it describes systematic writing that includes in 6 chapters.

1.1. Background

Monetary policy is a factor that influences an economic activity. It include in money market. One of variable that influence in the money market is interest rate, where interest rate has a relationship for investment. As a theory that explains the relationship of interest rate and investment by investment function. It shows there is negative relationship between interest rate and investment. It means an increase interest rate it will decrease investment. Like as we know, Interest rate is one instrument of monetary policy. Then, if a monetary policy can be better implemented so economic activity will good too. This can be decided by monetary policies that will be taken. The last will impact on macroeconomic targets. The target of

macroeconomics is to keep economic stability, which can be measured by opportunity job, price stability, and equilibrium of international payment. Same with the targets of macroeconomics, the monetary policy targets keep price stability, to push economic growth, and decreasing of the inflation rate.

The problem of inflation and economic growth are problems of each country. The both of the problems include in the targets of macroeconomics and monetary policy. There are many policies that taking to solve these problems. One of those policies likes as monetary policy, by monetary policy, we can push economic growth and control of the inflation rate. Monetary policy is one of a tool that used by government to reach macroeconomics goals according to Sadeghi, and Seyyed Yahya Alavi (2011).

Then, according to Onyeiwu (2012) monetary policy is a technique of economic management to bring economic growth and sustainable development that become a target of nations by a formal articulation where is how money affects on aggregate economics.

According to Nanga (2001: 180) monetary policy is a policy that implemented by monetary authorities with using the amount of money supply and interest rate to influence of aggregate demand level and reducing of instability in the economy.

According to Abata, Matthew Adeolu, Kehinde, and friends (2012) monetary policy have a freedom to control the money supply by monetary authorities (central bank with central government) to reach the targets of economics wanted. Same with

opinion by Junaidi (2005) he said that monetary policy can be run by the central bank to observe the amount of money supply in society. The central bank tries to control money supply because some of governments believe that the rates of money supply growth have an effect on inflation. Then, according to an analysis of Keynesian the excess of money supply growth will cause an increasing price level as continually, it means will be create of inflation according to Nanga (2001: 246).

From the all opinions things that monetary policy has an impact on the economy because the all opinion said that a monetary policy can be used to reach macroeconomics goals. So the point of monetary policy is to reach macroeconomic goals is to keep economy stability.

Other side an interest rate tool as monetary policy also will impact on economic growth because when interest rate decrease, money supply and economic growth will increase. In this case happen because the people, firms, and businesses more choose to invest, so an investment will increase. If an increase of investment it means development project can be executed. Then, it will be reduced on unemployment and increasing of economic growth and otherwise if money supply decreases so the interest rate will increase. An increasing of interest rate the people, firms, and businesses more choose to disinvest, but choose to save, so saving will increase and investment will decrease. Therefore, decreasing of investment means economic growth also decreases.

According to the explanations above, this research focuses on the relationship interest rate as monetary policy on inflation and economic growth in Indonesia during period 1983 - 2012. Based on the statistics report of Indonesia bank, Indonesia in the year 1983 until 2012 has an experience an increase and decrease in economic growth and also inflation. At the year 1983 was happened inflation is 11.8% and at the year 1998 where there is monetary and economy crisis so, inflation in Indonesia is 77.63% therefore, economic growth in Indonesia also decreases to be -13.13%. Then step by step to do until 2012, Indonesia effort to increase economic growth and control of inflation by using monetary policy and other policies. So that researcher interest to know the effect and the relationship monetary policy, inflation and economic growth in Indonesia. For that the writer conducts this research with entitled: **“MONETARY POLICY, INFLATION AND ECONOMIC GROWTH IN INDONESIA DURING PERIOD 1983 - 2012”**.

1.2. Research Problems

According to explanations of background above, the problems that will examine in this research are:

- (1) How the effect and relationship interest rate (BI rate) as monetary policy and inflation in Indonesia during period 1983- 2012?
- (2) How the effect and relationship interest rate (BI rate) as monetary policy and economic growth in Indonesia during period 1983 – 2012?

1.3. Research Objectives

Based on the research problems, the writer wants:

- (1) To know the effect and relationship interest rate (BI rate) as monetary policy and inflation in Indonesia during period 1983 – 2012.
- (2) To know the effect and relationship interest rate (BI rate) as monetary policy and economic growth in Indonesia during period 1983- 2012.

1.4. Research Advantages

The expected benefits of this research are:

- a. As an additional materials and complementary to previously existing research.
- b. As a supplementary study materials and literature for students of the Faculty of Economics Andalas University, especially for students of Economics Departments.
- c. To improve writer's ability in writing report and doing research especially in monetary.

- d. As references materials and information for further research, as well as to increase knowledge for writers.
- e. As an input for the benefit of the monetary authorities (government and central bank) or related agencies about monetary policy, inflation and economic growth in Indonesia in order make a good and effectively policies in the future.

1.5. Hypothesis

Gul, Khaid Mughal, dan Sabit Rahim (2012) hypothesis has significant role in the research to solve of problems in the research model. Hypothesis of this research can we look at the interest rate as monetary policy as follows:

- (1) There is positive relationship and significant effect of interest rate (BI rate) as monetary policy on inflation in Indonesia during period 1983 – 2012.
- (2) There is negative relationship and significant effect of interest rate (BI rate) as monetary policy on economic growth in Indonesia during period 1983 – 2012.

1.6. Systematical Writing

Chapter 1 is introduction that includes 6 subs - chapter like as background of problem, research problems, research objectives, research advantages, systematic writing and hypothesis.

Chapter 2 is theoretical framework and literature review. At discussion on theoretical frameworks divided into 3 subs - chapter like as theoretical framework, the targets of monetary policy and literature review.

Chapter 3 is research methodology divided into 4 sub - chapter that includes of kinds and sources data, definition of operational variable, analysis model, method of estimation and statistics test.

Chapter 4 is Indonesia economic development during period 1983 – 2012 divided into 2 sub – chapter such as the history of monetary policy in Indonesia, and the inflation, economic growth, and interest rate development in Indonesia.

Chapter 5 is result and discussion that explain about data analysis and discussion from the result of research. This chapter can be divided into 3 sub – chapter, the first is the estimation result, the second is assumption classic test and the last is discussion result.

Chapter 6 is closing that include conclusion and recommendation.