

## **ABSTRACT**

*Central government spending tends to increase year to year. The amount of tax revenue that is less than the expenditure encourages the government to obtain financing sources, one of which is the withdrawal of foreign debt. The foreign debt burden that is increasingly growing could affect Indonesian economy. Keynesian theory states expansionary fiscal policy will provide a positive impact on the national economy, which also resulted in an increase of aggregate consumption. On the other hand, the hypothesis of Ricardian or better known as Ricardian Equivalence Hypothesis (REH) states fiscal policy will not provide a meaningful impact on the economy because of the rational behavior of consumers. The aim of this study was to analyze the effects of fiscal policy and government foreign debt on consumption. This study also uses Gross Domestic Product (GDP) and wealth as factors affecting consumption. Data used in this study are secondary data obtained from Ministry of Finance, Statistics Indonesia and World Bank from 1973 to 2014. The analytical method used is the Error Correction Model (ECM).*

*The results showed that the fiscal policy variable through instrument of central government spending and interest payment on debt does not significantly affect consumption in the short-term. However, in the long-term, all independent variables used in this study showed a statistically significant effect on consumption. Ricardian Equivalence Hypothesis about the neutrality of fiscal policy does not apply in the Indonesian economy for period 1973 to 2014.*

*Keywords: Consumption, error correction model, fiscal policy, keynesian, ricardian equivalence hypothesis*