

ABSTRACT

This research analyzes the effectiveness of Indonesia's multi-tier cigarette excise tax policy in responding to the rising phenomenon of downtrading from SKM Tier I to Tier II products, a behavioral shift that increasingly threatens long-term revenue stability. As tobacco excise serve as the backbone of Indonesia's non-tax revenue, contributing more than 95 percent of total national excise receipts, understanding the interaction between tariff adjustments and economic conditions is critical within the framework of public economics and fiscal policy. Using quarterly data from 2017–2024, the research employs an interaction-based Ordinary Least Squares (OLS) model to analyze how GDP at current prices moderates the relationship between tier-specific excise rates and government revenue.

The empirical findings reveal clear asymmetries across tiers. Increases in Tier I excise rates significantly enhance state revenue, consistent with theoretical with the inelastic demand expected for premium cigarette. In contrast, higher Tier II excise rates produce a non-linear or negative revenue effect, reflecting intensified substitution toward cheaper products and confirming the relevance of cross-price elasticities and Laffer-curve dynamics within Indonesia's tiered market. The analysis further demonstrates that higher GDP strengthens the positive revenue impact of Tier I reforms while mitigating the adverse effects associated with Tier II tariffs.

Overall, the study concludes that Indonesia's complex tiered structure amplifies market distortions and limits the government's ability to capture optimal revenue. These results underscore the urgency for greater tariff harmonization and structural simplification to improve revenue performance and align excise policy with broader fiscal objectives.

Keywords: *Tobacco Excise, Downtrading, Multi-Tier Tax Structure, Fiscal Policy, Government Revenue, Laffer Curve.*

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