ABSTRACT

The persistent disparity in economic growth across Indonesian provinces indicates that regional fiscal policy plays an important role in determining regional economic performance. The degree of fiscal independence varies considerably across provinces, with most still dependent on central government transfers. Regional expenditure relative to GRDP also differs markedly across provinces, while empirical findings on its growth effect remain inconsistent. This study analyzes the effect of the degree of fiscal independence and regional expenditure on provincial economic growth in Indonesia during 2012-2024.

The study uses a quantitative approach with an unbalanced panel of 34 provinces over thirteen years, yielding 437 observations. The main independent variables are the ratio of locally generated revenue to total regional revenue as a proxy for the degree of fiscal independence, and the one-year lagged ratio of regional expenditure to GRDP. Control variables include investment, labor, the Human Development Index, the open unemployment rate, population growth rate, and a COVID-19 dummy for 2020-2021. The Chow and Hausman tests indicate the Fixed Effects Model with White period robust standard errors as the appropriate estimator.

Results show that the degree of fiscal independence has a positive and significant effect on provincial economic growth, while lagged regional expenditure has no significant effect despite its positive sign. Investment and labor have a positive and significant effect, while the Human Development Index, the open unemployment rate, and the COVID-19 dummy have a negative and significant effect on provincial economic growth in Indonesia.

Keywords: Economic Growth, Fiscal Independence, Regional Expenditure, Fiscal Decentralization, Indonesian Provinces