

The impact of fiscal decentralization on tourism development in Java Island: A study of district/city level data



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ABSTRACT

Java Island was the center of tourism activities in Indonesia and contributed the most to national tourist activity. However, the development of tourism among regions in Java Island still showed imbalances. Significant variations between regions indicated the need for a local-based approach to maximize tourism potential. In this context, fiscal decentralization plays an important role because it gives local governments more flexibility to manage local resources and design development policies according to the characteristics of their regions. This study aimed to analyze how fiscal decentralization influenced tourism development on Java Island and whether its impact differed across tourist segments. The analysis method used in this study was panel data regression with data from districts/cities during the 2010–2023 period. The results showed that fiscal decentralization contributed positively and significantly to the total number of tourists. However, there are differences in the impact between international and domestic tourists. Fiscal decentralization did not influence international tourist arrivals, but had a positive effect on domestic tourists. These findings indicated that the mechanism of strengthening regional fiscal capacity has not been able to attract international tourists, but it effectively stimulated domestic tourist movement through improvements in public services, local infrastructure, and tourism facilities. Thus, fiscal decentralization can be positioned as a strategic policy instrument to strengthen domestic tourism performance, while the development of international tourists required the support of macroeconomic factors and cross-regional policies that are not addressed at the district/city level.

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1. Introduction

Tourism is a strategic sector that has great potential to drive Indonesia's economic growth. As one of the world's most attractive destinations, Indonesia provides a diverse array of tourist destinations, from cultural diversity and natural beauty to abundant natural resources (Wahyuni & Gultom, 2024; Windyarto & Purnomo, 2024; Khasanah & Kurniawan, 2024). These advantages have led to an increase in tourist arrivals, as reflected in the rising number of visits to Indonesia each year. Total number of tourists in Indonesia continues to increase, as seen in the rise in international tourists from 10.23 million in 2015 to 11.67 million in 2023, along with domestic tourists growing from 256 million to 839 million visits in the same period. Among all regions in Indonesia, Java Island is the center of national tourism activities. In 2023, more than 73.2 percent of tourists were concentrated on Java Island (Statistics Indonesia, 2025) However, tourism development on Java Island is not entirely evenly distributed. Some areas, such as Batu City, Sleman Regency, and Tuban Regency, are developing rapidly with an average of more than 5 million visits each year. Meanwhile, other

areas such as Cimahi City, Salatiga City, and Banjar City are significantly lower, with an average of less than 100.000 visits per year.

The variations of tourism among regions illustrate that each region has different characteristics, potentials, and development needs. Therefore, the development of the tourism sector must be tailored to the conditions of each region so that the policies implemented can be more effective and precise in promoting tourism growth (Chen et al., 2020). To encourage equitable development and maximize regional potential, the role of local government is important because local governments are considered to have the best understanding of their regions (Deng et al., 2022; Oates, 1972). One mechanism that enables the government to play a role in promoting regional tourism is fiscal decentralization. In Indonesia, fiscal decentralization emerged through the implementation of regional autonomy reforms since 2001 (Djuniarti et al., 2023; Ihyani et al., 2025; Yunanda, 2025). Through fiscal decentralization, authority over revenue and expenditure is transferred to local governments so that it can be used to stimulate tourism development (Ul-Haq et al., 2023). Regions with high fiscal capacity are generally able to build better infrastructure, facilities, and tourism promotion than regions with low fiscal capacity.

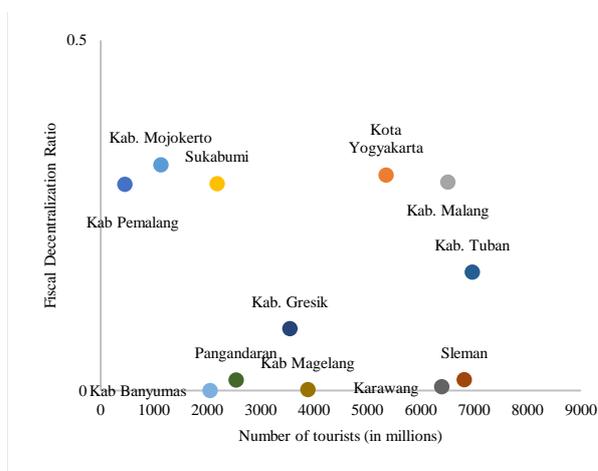


Figure 1A. The Association between Fiscal Decentralization Ratios and Number of Tourists in 2010

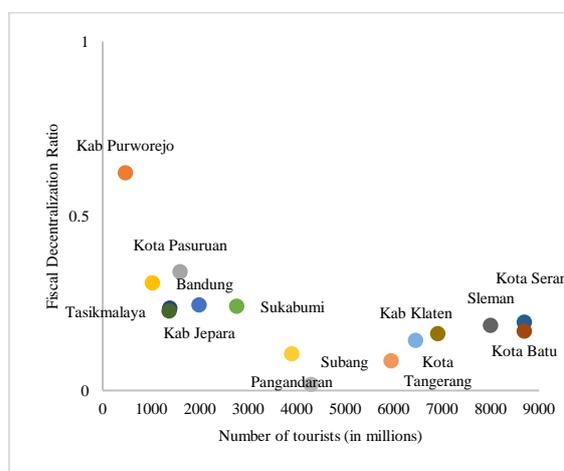


Figure 1B. The Association between Fiscal Decentralization Ratios and Number of Tourists in 2023

Figure 1A and Figure 1B shows an interesting pattern between fiscal decentralization and tourist visits to Java Island. Regions with high fiscal decentralization ratios, such as Mojokerto Regency and Purworejo Regency, have low tourist visits. Conversely, regions such as Sleman Regency and Magelang Regency with low fiscal decentralization ratios have high tourist visits. This condition shows that although fiscal decentralization should provide budget flexibility to support the tourism sector, in fact the relationship between these two variables is not always linear. This phenomenon is interesting to analyze further in terms of how fiscal decentralization affects tourism development on Java Island.

Studies investigating the connection between fiscal decentralization and tourism has been conducted in several countries without consistent results. In some studies, fiscal decentralization has been found to enhance tourism development (Solarin, 2024; Tao et al., 2024; Ul-Haq et al., 2023). These results are in line with studies showing that fiscal decentralization promotes economic growth in general (Marya & Handra, 2024; Simanjuntak, 2015). However, Zeng et al (2020) found the opposite result, that higher fiscal decentralization actually harms tourism development. This result is supported by the findings of Hardianto et al (2024), which show that fiscal decentralization actually causes a decline in economic growth. Meanwhile, Chen et al (2020) found that fiscal decentralization has different impacts between regions with high and low fiscal autonomy.

Despite the growing body of literature on fiscal decentralization and tourism, several important gaps remain. First, most existing studies are conducted at the national or provincial level, which limits the understanding of local heterogeneity at the district/city level. Second, empirical research in Indonesia on tourism determinants predominantly focuses on macroeconomic factors such as environmental quality, exchange rates, interest rates, and infrastructure (Raharjo et al., 2023;

Sugianto, 2022; Suharyono & Digidowiseiso, 2020; Wahyuni & Gultom, 2024; Wicaksono, 2022). In contrast, research on the impact of fiscal decentralization in Indonesia has largely concentrated on macroeconomic indicators, such as economic growth and interregional disparities, leaving its role in tourism development relatively underexplored. Third, tourism is commonly treated as a single aggregate indicator, without distinguishing between international and domestic tourist segments, even though these groups are driven by different economic and institutional mechanisms.

This study addresses these research gaps by providing district/city-level empirical evidence from Java Island and by explicitly examining the differential impact of fiscal decentralization on international and domestic tourists. This segmentation-based approach offers a novel perspective on how local fiscal capacity translates into tourism performance, thereby contributing new empirical insights to the literature on fiscal decentralization and tourism development in developing countries. Building on these contributions, this study examines the impact of fiscal decentralization on tourism development in Java Island over the period 2017–2023. Specifically, it addresses the following research questions: (1) Does fiscal decentralization influence tourism development in Java Island? (2) Is there a difference in the effect of fiscal decentralization on the number of international and domestic tourists in Java Island?. There are two contributions of this study, namely: 1) This study uses panel data for the period (2017–2023) for districts/cities on the island of Java, thereby capturing the temporal and regional dynamics in the relationship between fiscal decentralization and tourism. 2) This study compares the impact of fiscal decentralization on two types of tourists, to analyze the differences in the effects of fiscal decentralization on each tourism segment. These contributions will provide a theoretical basis for promoting better tourism development on Java Island.

2. Literature Review

2.1. The Relationship Between Fiscal Decentralization and Tourism

The Fiscal Federalism theory by Oates (1972) posits that every public service, such as tourist destinations, should be provided by the authority with jurisdiction over the smallest geographical area because it is able to internalize the benefits and costs of providing such services. Local governments have geographical and informational advantages that enable them to better understand the ecological environment of their regions (Tao et al., 2024; Yu et al., 2014). Fiscal decentralization policies give local governments the right and responsibility to regulate and manage their own budgets, such as collecting taxes and levies, and allocating regional expenditure in accordance with their regional development (Hyman, 2010; Zeng et al., 2020). Indonesia has implemented decentralization since 2001 through Law No. 22 and Law No. 25 of 1999 (Simanjuntak, 2015). With this policy, regions have greater control over the direction of development, one of which is in the development of the tourism sector (Handini et al., 2025).

Fiscal decentralization expands the independent authority of local governments to improve efficiency and effectiveness in managing fiscal revenue and expenditure to support economic growth (Yunanda, 2025). As one of the strategic areas in promoting economic growth, local governments will strengthen tourism allocation by encouraging economic actors to enter the tourism industry, accelerating the flow and allocation to the tourism industry, and creating new business models for tourism (Tao et al., 2024). Fiscal decentralization also allows local governments to design environmental governance policies in line with sustainable development needs, which in turn can strengthen the competitiveness of tourist destinations, strengthen the image of tourism, and increase tourist interest in visiting (Ul-Haq et al., 2023). In addition, fiscal decentralization will improve tourism performance by stimulating competition between regions (Guccio et al., 2018). This competition encourages regions to innovate in strengthening regional tourism development infrastructure, increasing human resource capacity, and improving public services such as transportation, culture, and entertainment, thereby expanding the scale of tourism inflows (Umam, 2025).

2.2. Previous Research

Previous studies on the relationship between fiscal decentralization and tourism have shown mixed results. Tao et al (2024) used panel data analysis with various robustness tests such as different variable sizes, Systematic GMM (SYS-GMM), and spatial autoregressive (SAR) models. The findings show that fiscal decentralization consistently promotes inbound tourism in China in the period 2005-2020. Furthermore, Solarin (2024) used a panel quantile regression method and found

that fiscal decentralization led to an increase in tourist arrivals in 10 countries. The research by [Ul-Haq et al \(2023\)](#) also shows that fiscal decentralization contributes to tourism growth in the United States, the United Kingdom, Japan, Germany, France, and China during the period 1996-2018.

On the other hand, [Chen et al \(2020\)](#) found that between 1993 and 2018 in China, the effect of fiscal decentralization on tourism exhibited considerable heterogeneity. In regions with higher fiscal autonomy, government spending was directed towards promoting tourism development. In contrast, in provinces with lower fiscal autonomy, fiscal decentralization contributed more to enhancing social equity than to advancing tourism development. Furthermore, [Zeng et al \(2020\)](#), using panel data regression analysis, found that fiscal decentralization encouraged local governments to develop companies and industries that pollute the environment, thereby supporting long-term tourism growth.

Research by [Yu et al \(2014\)](#) in China shows that fragmented decentralization is the root cause of spatial imbalances in regional tourism development. [Guccio et al \(2018\)](#) analyzed the impact of decentralization on the efficiency of tourist destinations in Italy. The findings showed that decentralization reduced the efficiency of tourist destinations. It is due to weak institutional capacity and coordination between levels of government after policy devolution. Based on various previous studies, it can be concluded that the findings have not shown consistency, so research on the impact of fiscal decentralization on tourism still needs to be continued. The absence of similar studies in Indonesia makes this research even more important. Therefore, this study focuses on Java Island, which is the center of tourism activities in Indonesia.

2.3. Conceptual Framework and Hypothesis Development

[Figure 2](#) illustrates the research framework model that places Tourism as the dependent variable, while fiscal decentralization is the independent variable. Fiscal decentralization provides political and economic incentives for local governments, which in this study are district/city governments. Political incentives encourage local leaders to strengthen local economic performance as a form of achievement that affects their political position and reputation ([Xin & Qian, 2022](#)). Meanwhile, from an economic perspective, fiscal authority provides opportunities for local governments to optimize public revenue and expenditure in accordance with the potential of their regions, thereby encouraging competition among regions to improve their economic base.

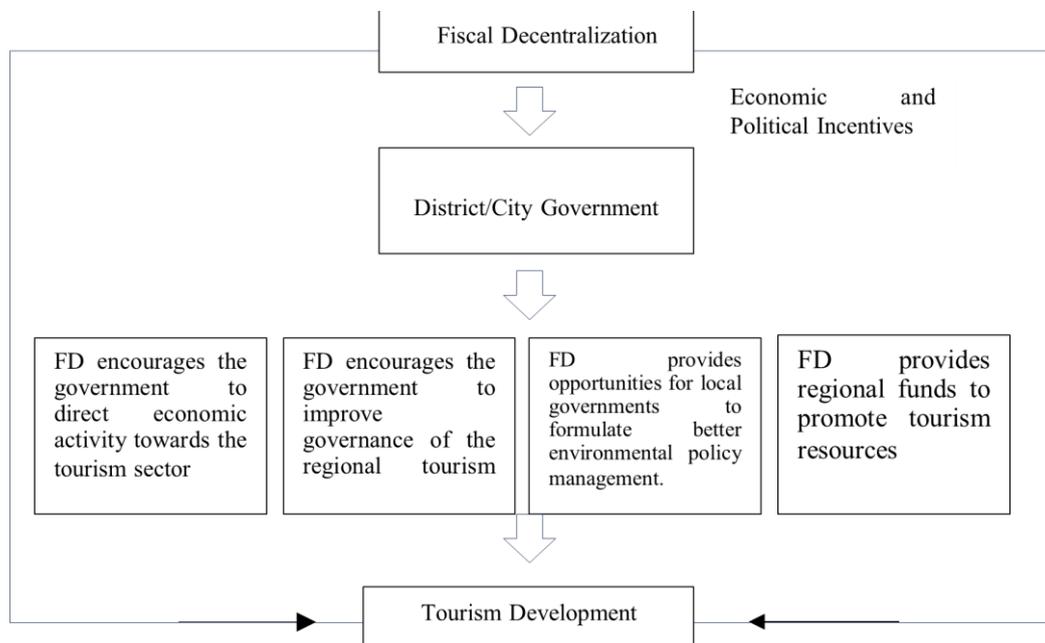


Figure 2. Conceptual Framework

With these political and economic incentives, local governments will be encouraged to improve development performance through sectors that have a significant fiscal and economic impact, one of which is the tourism sector. Through their fiscal authority, local governments can play an active role in directing economic activity towards the tourism sector, accelerating the flow of resources between tourism sub-sectors, and creating new innovations and business models that can attract regional investment. These efforts are realized through improvements in tourism, cultural, and entertainment

infrastructure, strengthening destination management, and sustainable environmental management and ecotourism development (Tao et al., 2024). Ultimately, these various efforts can encourage regional tourism development and attract tourists to the region. Therefore, the first hypothesis proposed is:

H1: Fiscal decentralization influences the tourism development on Java Island.

Although fiscal decentralization is expected to affect tourism development, its impact may not always be the same across all types of tourists. The tourism structure of Java Island consists of two groups of tourists, namely foreign tourists and domestic tourists, and the factors that influence them may be different. This is because these two groups have different characteristics, preferences, and sensitivities. Therefore, the second hypothesis proposed is:

H2: Fiscal decentralization has different effects on international tourists and domestic tourists on Java Island.

3. Method

3.1. Data and Sources

The dependent variable in this study was total tourist visits, while fiscal decentralization was positioned as the independent variable. Fiscal decentralization was measured by the ratio of tourism expenditure to total tourism expenditure at all levels of government, including regencies/cities, provinces, and the central government in Indonesia. In this study, tourist visit data were obtained from Statistics Indonesia (BPS, 2025). Meanwhile, fiscal decentralization data were obtained from the Ministry of Finance of the Republic of Indonesia (Kemenkeu RI). To analyze the differences in the effects of fiscal decentralization on each type of tourist, tourists were grouped into two categories: international tourists and domestic tourists. Table 1 presents the operational definitions and measurements of each variable used in this study.

Table 1. Operational Definitions

Variable	Symbol	Definition	Measurement
Dependent Variable			
Total Number of Tourists	Total of tourists	Total number of tourist visits (Person)	Number of visits (persons)
International Tourists	International Tourists	Number of international tourist arrivals	Number of arrivals (persons)
Domestic Tourists	Domestic Tourist	Number of domestic tourist visits	Number of visits (persons)
Independent Variable			
Fiscal Decentralization	FD	Degree of fiscal autonomy in tourism expenditure	Ratio of district/city tourism expenditure to total tourism expenditure of all government levels (%)
Control Variable			
Economic growth	GRDP	Regional economic performance	GRDP per capita (rupiah)
Tertiary Industry Structure	IS	Share of tertiary (service) sector in regional economy	Natural logarithm of tertiary sector output share (%)
Accommodation	AK	Tourism accommodation capacity	Natural logarithm of total hotel rooms (units)
Transportation infrastructure	TP	Regional accessibility infrastructure	Natural logarithm of road length to land area ratio (%)

Source: multiple sources

According to Cheng et al (2024); Dong et al (2019); Raharjo et al (2023); Suharyono & Digdowiseiso (2020); Sun et al (2025); Tao et al (2024); Zeng et al (2020), economic growth, tertiary industry structure, accommodation, and transportation infrastructure are control variables in this study. Various control variables in this study were obtained from Statistics Indonesia (BPS). This

study used a sample of 91 districts/cities on the Java Island, selected based on the completeness and consistency of data availability throughout the period 2017–2023.

3.2. Analysis Techniques

The analytical tool used to estimate the impact of fiscal decentralization on international tourist arrivals is a panel data regression analysis. The model of the panel data regression equation with total tourist arrivals is written as follows:

$$\text{Total Number of Tourists} = \alpha_0 + \alpha_1 FD + \alpha_2 Z_{it} + e \quad (1)$$

Meanwhile, the equation model with international tourist visits is as follows:

$$\text{International Tourists} = \beta_0 + \beta_1 FD + \beta_2 Z_{it} + e \quad (2)$$

Finally, the equation model with domestic tourist visits is as follows:

$$\text{Domestic Tourists} = \gamma_0 + \gamma_1 FD + \gamma_2 Z_{it} + e \quad (3)$$

Where FD_{it} represents the fiscal decentralization ratio; while Z_{it} represents control variables consisting of Economic Growth ($GRDP_{it}$); Tertiary Industry Structure (IS_{it}); Accommodation (AK_{it}); and Transportation Infrastructure (TP_{it}). Finally, e_{it} represents the error term.

4. Results and Discussion

4.1. Estimation Results

Table 2 shows the statistical description of the variables in this study. The average total number of tourists reached 1.828.665 visits. Meanwhile, the average number of international tourists was 22.564 visits, while the average number of domestic tourists reached 1.806.101 visits. The average value of fiscal decentralization, GRDP per capita, industrial structure, accommodation, and transportation infrastructure are as follows: 0.098874; 35539.94; 3.822101; 7.203997; 0.167641.

Table 2. Descriptive Statistics

Variable	Obs	Mean	Std Dev.	Min	Max
Total Number of Tourists	637	1828665	3349424	0	51800000
International Tourists	637	22564.13	108774.4	0	2176487
Domestic Tourists	637	1806101	3330962	0	51700000
Fiscal Decentralization	637	0.098874	0.105691	0	0.833335
GRDP Per capita	637	35539.94	38681.16	11947	751010
Tertiary Industry Structure	637	3.822101	0.38706	0	4.454216
Ln_Accommodation	637	7.203997	1.089316	4.465908	10.14596
Ln_Transportation infrastructure	637	0.167641	0.816346	-1.33477	2.518138

Source: data processed

The Chow test results for each research model show that the cross-section F probability is less than 5% significance level, so the best model among the three models is the Fixed Effect Model (FEM). The results of the Hausman test show that the probability values for all three models are below the 5% significance level, so the most appropriate model to use is the Fixed Effects Model (FEM). Furthermore, the multicollinearity test results show that the VIF values of all variables are less than 0.80, shows that there is no multicollinearity between independent variables. Meanwhile, the heteroscedasticity test results for the three models have a probability of less than 5% significance level, indicating that there is heteroscedasticity in the research model. To overcome this problem, the method used is robust standard error (Napitupulu et al., 2021).

Table 3 shows the results of robust standard error estimation with fiscal decentralization as the main variable in the estimation model. Column 1 shows that there is a positive effect of fiscal

decentralization total tourist arrivals. Meanwhile, column 2 shows no effect on international tourist arrivals, and column 3 highlights a positive influence on domestic arrivals.

Table 3. Estimation Results Excluding Control Variables

Variables	Total Number of Tourists	International Tourists	Domestic Tourists
	(1)	(2)	(3)
FD	3.882e+06** (1.889e+06)	35.708 (74.122)	3.846e+06** (1.871e+06)
Constant	1.445e+06*** (186.795)	19.034** (7.329)	1.426e+06*** (185.009)
Diagnostic Tools			
Observations	637	637	637
R-squared	0.012	0.001	0.012
Number of id	91	91	91

Source: data processed

Subsequently, in [Table 4](#), control variables consisting of economic growth, tertiary industry structure, number of accommodations, and transportation infrastructure were added to the estimation model. The results show that the effect of decentralization remains consistent and does not change significantly with the estimation model without the control variables.

Table 4. Estimation Results Including Control Variables

Variables	Total Number of Tourists	International Tourists	Domestic Tourists
	(1)	(2)	(3)
FD	3.763e+06** (1.822e+06)	44.409 (75.544)	3.718e+06** (1.802e+06)
GRDP	3.705** (1.446)	-0.0247 (0.0458)	3.730** (1.481)
Ln_IS	375.062** (158.531)	-2.066 (5,294)	377.128** (162.130)
Ln_AK	627.183 (1.045e+06)	-23,].621 (16,180)	650.804 (1.043e+06)
Ln_TP	-519.697 (634.302)	7.681 (10.052)	-527.378 (634.068)
Constant	-4.540e+06 (7.691e+06)	195.825 (117.926)	-4.735e+06 (7.677e+06)
Diagnostic Tools			
Observations	637	637	637
R-squared	0.017	0.004	0.017
Number of id	91	91	91

Noted: ***, **, and * significantly at 0.01, 0.05, and 0.1

4.2. The Impact of Fiscal Decentralization on Total Tourist Visits

[Table 3](#) and [4](#) shows the fiscal decentralization has a positive effect on the total number of tourist visits to Java Island. It means that the higher the fiscal decentralization ratio of a region, the higher the total number of tourist visits received by that region. These results support the initial hypothesis that fiscal decentralization has an impact on regional tourism development. The results of this study are also consistent with the findings of [Tao et al \(2024\)](#) and [Solarin \(2024\)](#), who found that fiscal decentralization encourages an increase in tourist arrivals through strengthening fiscal capacity and improving the quality of tourism services. Higher allocation of expenditures for tourism sector is one of the instruments that can be used to strengthen the attractiveness of a region's destination through infrastructure development, promotion, and improvement of tourism facilities.

This finding is in line with [Oates \(1972\)](#), who states that tourism destinations as public services should ideally be managed by the smallest jurisdiction, namely the district/city government. The district/city government has a better understanding of the characteristics of its region than the

provincial or central government. When tourism spending is directed appropriately in line with local needs, it will encourage tourism development. For example, local governments are aware of access limitations in a regional destination, so they allocate tourism spending to improve infrastructure in that area. When access is adequate, it will attract tourists to visit and increase tourism activities, which will ultimately drive regional economic growth.

Fiscal decentralization reflects the independence of local governments and represents a fiscal system in which the central government grants a certain degree of autonomy to local governments in terms of fiscal revenue and expenditure. Local governments can prioritize tourism by promoting it through their fiscal authority. Governments can allocate local spending to tourism spending to improve the infrastructure for tourism, culture, and entertainment in their regions. Improving the infrastructure for tourism, culture, and entertainment will increase the attractiveness of a region, which will ultimately increase the total number of tourist visits.

Furthermore, regarding the impact of control variables on total tourist visits (Table 4), there is a significant positive relationship between per capita GRDP and total tourist visits. These results are in line with the research of Zeng et al (2020); Q. Sun et al (2023) and Suharyono & Digdowiseiso (2020), which found that regions with good economic growth will encourage the development of various facilities and infrastructure, such as transportation, communication and information networks, hotels, restaurants, and entertainment centers (F. N. Hardianto, 2023). Ultimately, this will be more attractive to tourists, thereby attracting tourists to visit (F. N. Hardianto, 2023). The tertiary industry structure also has a positive influence on total tourist visits, because the industrial composition of a region not only shapes the external environment for the development of inbound tourism, but is also closely related to the region's capacity to provide tourism services (Tao et al., 2024). The dominance of the tertiary industry, especially in the transportation, communication, accommodation, and financial services sectors, will provide facilities and services that cater to tourist comfort. Meanwhile, hotel room accommodation and transportation infrastructure have no effect on total tourist visits. These findings are inconsistent with the research by Hor (2021), which found that hotel rooms have an effect on tourist visits, and Raharjo et al (2023), which found that transportation infrastructure has an effect on tourist visits. These results indicate that the physical facilities in this region are already relatively evenly distributed and adequate, thus an increase in the number of accommodations or additional infrastructure no longer has a direct impact on increasing tourist visits.

4.3. The Difference in the Impact of Fiscal Decentralization on International Tourist and Domestic Tourists

After conducting tests with different estimation models, the results of the study show that there is a difference in the effect of fiscal decentralization on international tourists and domestic tourists in Java Island. These results support hypothesis two, namely that there is a difference in the effect of fiscal decentralization on international tourists and domestic tourists. In the first model, fiscal decentralization had no effect on international tourists, while in the second model, fiscal decentralization was found to have a positive effect on domestic tourists. This difference can be explained by the characteristics of the two tourist types. Increasing regional fiscal capacity through tourism spending allocations has not been able to directly attract international tourists. This situation arises because the decision to visit by international tourists is generally more influenced by macroeconomic and global factors such as the exchange rate of Indonesian Rupiah, trade openness, inflation rate, and the gross domestic product (GDP) of the tourists' home countries, which cannot be measured at the district/city level (Hor, 2021; Muryani et al., 2020; Nairizi et al., 2024). It is also the reason why all control variables such as regional economic growth, industrial structure, number of accommodations, and transportation infrastructure also have no effect on international tourist visits.

Unlike foreign tourists, the second estimation model shows that fiscal decentralization positively affects domestic tourists. It means that the higher the fiscal capacity of the region, the greater the number of domestic tourists visiting. It also confirms that fiscal decentralization effectively boosts domestic tourism through the provision of infrastructure, promotion, and cultural activities managed by local governments. Furthermore, the control variables that have an effect on domestic tourists are per capita GRDP and the tertiary industry structure. Regions with higher incomes and a dominance of the service sector have stronger economic support for developing tourism facilities. Meanwhile, the number of hotel rooms and transportation infrastructure do not significantly affect domestic tourists, possibly because domestic tourists tend to take short trips (one-day trips), such as trips between districts/cities within a province. Therefore, the need for formal accommodation is relatively low.

5. Conclusion

The finding of the study align with the initial hypothesis that fiscal decentralization affects tourism development in Java Island. Based on regression analysis of district/city level data, an increase in regional financial capacity has been proven to encourage the provision of better infrastructure, facilities, and tourism promotion, thereby strengthening tourist movement at the regional level. However, when differentiated by tourist type, this effect is only significant for domestic tourists. It suggests that domestic tourists are more responsive to improvements in facilities and local economic activities, while international tourist visits are more dependent on external factors such as inflation, exchange rates, and the level of economic openness of a region..

To encourage tourism growth at the district/city level in Java Island, local governments need to develop more strategic fiscal planning so that public spending allocations truly support the strengthening of the tourism sector. Although this study has provided an overview of the role of decentralization in promoting tourism in Java Island, there are a number of limitations that need to be considered. First, this study is still limited to 91 districts/cities on Java Island due to data availability. Second, this study only uses four control variables, ignoring several other factors that may affect tourism. Therefore, further research is needed to overcome these limitations.

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