OPEN ACCESS

Saudi Journal of Economics and Finance
Abbreviated Key Title: Saudi J Econ Fin
ISSN 2523-9414 (Print) |ISSN 2523-6563 (Online)
Scholars Middle East Publishers, Dubai, United Arab Emirates
Journal homepage: http://saudijournals.com

Original Research Article

The Impact of Regional Financial Capability during the COVID-19 Pandemic towards Regional Fiscal Capacity

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DOI: 10.36348/sjef.2022.v06i02.006 | **Received:** 11.01.2022 | **Accepted:** 14.02.2022 | **Published:** 26.02.2022

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Abstract

Regional fiscal capacity is the region's ability reflected in regional revenue, consisting of own-source revenue (PAD), fiscal balance transfers, and other legitimate regional revenues. This study aims at analysing the impact of regional financial capability during the Covid-19 Pandemic towards regional fiscal capacity. The research was conducted in local governments in Indonesia during 2020 using descriptive qualitative analysis. The results showed that generally the Covid-19 Pandemic affected the reduction on own-source revenue (PAD) in almost all provinces in Indonesia during the first semester of 2020. From 66 regencies/cities as the sample from this research, 49 regencies decreased in revenue and expenditure because of the Covid-19 Pandemic. The revenue reduction in each region was caused by regional taxes reduction of around 2,5 percent and 10,68 percent sequentially in the first semester of 2020, fiscal balance transfers around 8,42 percent, and general allocation grant (DAU) around 9,8 percent and 6,94 percent. Meanwhile, to solve the regional fiscal problems, the local governments implemented 2 types of policies: (1) the first policy is to implement a counter-cyclical policy through maintaining economic stability, decreasing revenues, and increasing local government expenditures; (2) the second policy is to implement a pro-cyclical policy through increasing revenues and decreasing expenditures. The present research also found that regencies/cities that implemented a counter-cyclical policy generally increased in expenditure components, such as grant expenditure around 316,51 percent and regional capital expenditure. Some local governments built infrastructure (assets and buildings) during the Covid-19 Pandemic. However, local governments decreased around -1% - 16% for the employee expenditures.

Keywords: Regional Financial Capability, the Covid-19 Pandemic, Regional Fiscal Capacity.

BACKGROUND

Nowadays, the government in Indonesia consists of the central and regional governments. The central and regional governments are also demanded to have the ability to result funds used to fund their necessity. Normally, it can be seen from the regional financial capacity to measure the success. According to the Regulation of the Minister of Finance Number 120/PMK.07/2020, regional financial capacity is the ability of each region reflected in regional revenue minus by the revenue that the usage has been determined and regular expenditures. Meanwhile, according to the Regulation of the Minister of Home Affairs Number 62 of 2017, regional financial capacity is the classification of region to determine the class of regional financial capability determined by the formula as the basis of calculation for the total of intensive communication allowance, recess allowance, and leaders' operational funds. The policies governing regional financial capacity include two regulations, those are (1) the Regulation of the Minister of Home Affairs Number 62 of 2017 concerning Classification of Regional Financial Capability, the Implementation and Accountability of Operational Funds; and (2) the Regulation of the Minister of Finance Number 120/PMK.07/2020 concerning Regional Fiscal Capacity Mapping.

The regional financial capability is going to affect towards the regional fiscal capacity. Then, what is meant by regional fiscal capacity? Regional fiscal capacity is the financial capacity of each regency/city reflected in regional revenue minus by the revenue that the usage has been determined and regular expenditures (the Regulation of the Minister of Finance Number 120/PMK.07/2020). Meanwhile, according to Hyman (2011:708), fiscal capacity is the ability of a region to fund public services provided by the government. In particular, regional fiscal capacity in 2020 is regulated by the Regulation of the Minister of Finance Number 120/PMK.07/2020.

Based on the reality, regional financial capability consists of 3 (three) classifications. Those are: high, medium, and low. Based on the Regulation of the Minister of Home Affairs Number 62 of 2017, the regional financial capability classification determination is calculated based on the total of regional general revenue minus by local government's employee expenditures. Furthermore, the provincial financial capability is classified as follows:

a) more than four trillion five hundred billion rupiah is classified as the high regional financial capability;
b) one trillion four hundred billion rupiah up to four trillion five hundred billion rupiah is classified as the medium regional financial capability, and
c) Under one trillion four hundred billion rupiah is classified as the low regional financial capability.

Meanwhile, regency/city financial capability is also classified into 3 (three) classifications. The three classifications aforementioned are stated as follow:

a) More than five hundred and fifty billion rupiah is classified as high regional financial capability;
b) Three hundred billion rupiah up to five hundred fifty billion rupiah is classified as the medium regional financial capability, and
c) Under three hundred billion rupiah is classified as the low regional financial capability.

The capability of regional financial classifications aforementioned certainly decreased during the Covid-19 Pandemic in 2020. According to the official report from the Impact of the Covid-19 Pandemic on Subnational Finances as quoted by Tan (2021: 44), it was stated that the impact of the Covid-19 Pandemic significantly influenced towards the reduction of regional fiscal capacity around 10% and the increase of regional expenditures around 5%. Thus, in 2020 both the center and the local governments experienced a budget deficit. This phenomenon effected the amount of fiscal balance transfers to the local governments. The policy is stated in Presidential Regulation Number 54 of 2020 which was strengthened by the Regulation of the Minister of Finance Number 19/PMK.07/2020, in which the total of general allocation grant (DAU) was Rp427.1 trillion to be Rp384.4 trillion. In addition, the total of profit-sharing grant (DBH) was Rp117.6 trillion to be Rp89.8 trillion. Finally, the total of spesific purpose grant (DTK) was Rp202.5 trillion to be Rp183 trillion.

The results of several previous research explain the phenomenon above, such as the research undertaken by Widani & Erawati (2016) which showed that own-source revenue (PAD) and general allocation grant (DAU) have negative and unsignificant effect on human development index (IPM). Meanwhile, profit-sharing grants have a positive but insignificant impact on the human development index. Afterwards, regional economic growth has a positive and significant effect on human development index of regencies/cities in Bali Province. In addition, the research undertaken by Tan (2021) found that the Covid-19 Pandemic had threatened the regional fiscal health. The real threat decreased the realization of regional revenues, so that regional cash flows were obstructed, and some regional priority expenditures were delayed. Thus, the situation caused the current budget deficit in 2020. This was the global phenomenon faced by local governments in Indonesia.

Furthermore, Triarda & Damayanti (2021) found that economic development had changed the regional potential. This phenomenon was seen in some tax sectors that cannot be used longer as reliable sectors if they were still managed with the conventional paradigm. The economic development in the city of Malang had produced a new prima donna in local taxes, such as in hotels and restaurants.

Based on the phenomenon above, this research aims at explaining the impact of Covid-19 Pandemic towards the regional fiscal conditions and regional fiscal capacity in 2020. This research hopefully can figure out the regional fiscal conditions during the Covid-19 Pandemic and regional efforts to solve the impact of the Covid-19 Pandemic on regional financial conditions.

RESEARCH METHOD

The present research employs qualitative method through descriptive approach (Creswell, 2012). Descriptive approach is included in narrative research that is commonly used in qualitative research. Thus, the qualitative descriptive method is understood as a method at which researchers proceed with the data collection based on the results of identification on how social phenomena happened (Winartha, 2006; Iskandar, 2013).

The researcher describes the situation in the research field by referring to the regional financial capability during the Covid-19 Pandemic for local governments in Indonesia. There are two techniques used as follow:

1. Observation technique at which the researcher observed the conditions and activities in the research field that is stated in government's report documents.
2. Documentation technique at which the researcher collected information obtained from relevant

institutions. Besides that, the researcher searched for other documents from the internet in line with the relevant data reffering to regional financial capability and regional fiscal capacity in Indonesia.

In describing the data, the researcher presents them in a graph or a chart. Then, the data are described according to the conditions occurred in the research field during the Covid-19 Pandemic in 2020.

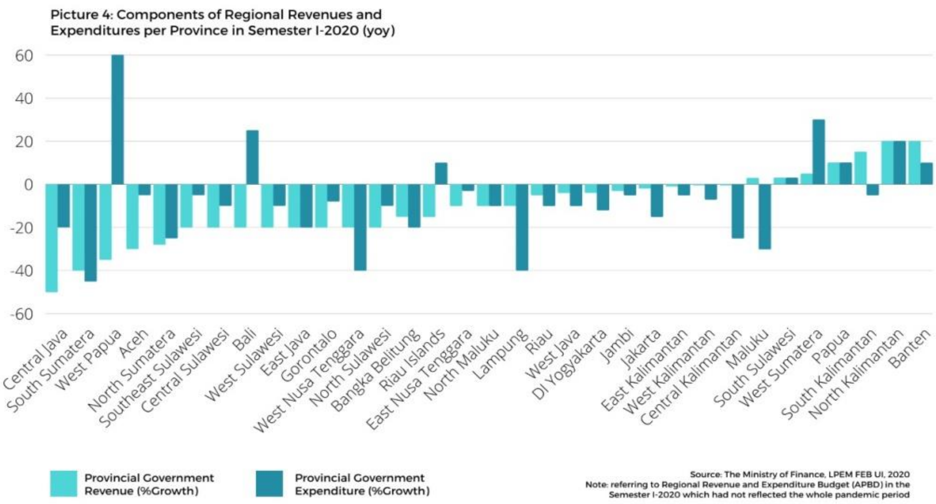
RESULTS AND DISCUSSION

Results

The data referring to regional financial capability during the Covid-19 Pandemic were cited from the research conducted by the Economic Research Division of PT. SMI during 2020. The regional financial capability during the Covid-19 Pandemic is reported as follows.

Common Condition of Regional Fiscal during Covid-19 Pandemic

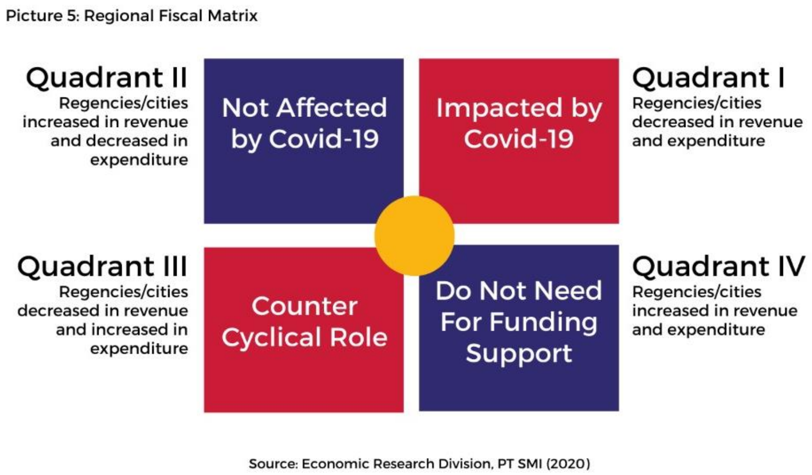
The Covid-19 Pandemic decreased provincial revenues and expenditures in Indonesia in the first semester of 2020 (yoy). However, several provinces such as Banten, North Kalimantan, Papua, and West Sumatera increased in provincial revenues and expenditures. The common condition of provincial fiscal during the Covid-19 Pandemic could be seen in the following graph.



Source: Economic Research Division PT. SMI., 2020: 147-148

The Framework of Regional Fiscal Mapping

Regional fiscal mapping was implemented based on the data on the realisation of regional revenues and expenditures in the first semester of 2020 compared by the first semester of 2019. The regional fiscal matrix was used to map the regional budget and fiscal policy condition, notably at the regency/city level during the Covid-19 Pandemic. Regional fiscal mapping was divided into four quadrants as asserted in the following chart.

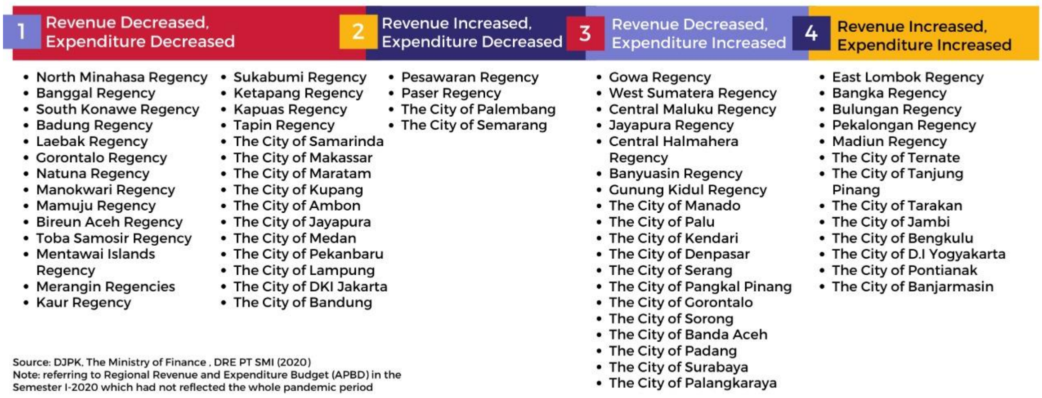


Source: Economic Research Division PT. SMI., 2020: 149

Regional Fiscal Mapping during the Covid-19 Pandemic

Based on the data in the first semester of 2020, regional fiscal mapping indicated that most regencies/cities located in quadrant I gained reduction on revenue and expenditure caused by Covid-19 Pandemic. From the research sample of 66 regencies/cities, 30 regions located in quadrant I decreased their revenue and expenditure caused by the Covid-19 Pandemic. Furthermore, 19 regencies/cities located in quadrant III implemented a counter-cyclical policy through maintaining economic stability, decreasing revenues, and increasing local government expenditures. The reduction revenues from each region in quadrants I and III were caused by the reduction on regional taxes around 2,5 percent (yoy) and 10,68 percent (yoy) sequentially in the first semester of 2020, fiscal balance transfers around 8, 42 percent (yoy), and general allocation grant (DAU) around 9,8 percent (yoy) and 6,94 percent (yoy) sequentially. Then, only 4 regions located in quadrant II implemented a pro-cyclical policy by increasing revenues and decreasing expenditures. Finally, 13 regencies/cities located in quadrant IV were not affected by the Covid-19 Pandemic. The regions above in quadrant IV increased their revenue and expenditure during the Covid-19 Pandemic. These aforementioned phenomena are pointed out in the following chart.

Picture 6: Mapping Result by means of Regional Fiscal Matrix



Source: Economic Research Division PT. SMI., 2020: 150-151

The Components of Regional Income

The components of regional income were in regional taxes, fiscal balance transfers, and general allocation grant (DAU). The reduction revenue of the regencies/cities located in quadrants I and III was caused by the reduction on their regional taxes around 2,5 percent (yoy) and 10,68 percent (yoy) sequentially in the first semester of 2020, fiscal balance transfers around 8,42 percent (yoy), and general allocation grant (DAU) around 9,8 percent (yoy) and 6.94 percent (yoy) sequentially. However, some regencies/cities in quadrants I and III increased their specific allocation grant (DAK). These phenomena are pointed out in the following chart.

Table 1: Cities & Regencies Revenue during Semester I-2020

Revenue	Quadrant I	Quadrant II	Quadrant III	Quadrant IV
	Growth Average (yoy)	Growth Average (yoy)	Growth Average (yoy)	Growth Average (yoy)
Total Revenue	-15,6%	17,67%	-10,40%	5,98%
Own-Source Revenue (PAD)	10,3%	31,55%	-0,16%	2,33%
Tax	-2,5%	23,62%	-10,68%	-2,94%
Retribution	3,9%	8,68%	5,87%	-3,25%
Fiscal Balance Transfers (Dana Perimbangan)	-10,6%	6,05%	-8,42%	0,81%
Profit Sharing Grant (Dana Bagi Hasil)	-2,0%	50,30%	-5,87%	59,20%

Source: Economic Research Division PT. SMI., 2020: 151-152

The components of regional expenditure were in social aids, grant expenditures, and regional capital expenditures. On the average, during the Covid-19 Pandemic regencies/cities located in all quadrants increased their social aid components and grant expenditures around 316,51 percent (yoy). Afterwards, regional capital expenditures increased in quadrants I, III, and IV which meant that some local governments were still able to build infrastructure (assets and buildings) during the Covid-19 Pandemic. However, local governments decreased around -1% - 16% for the employee expenditures. The following chart shows the components of regional expenditure such as social aids, grant expenditures, and regional capital expenditures.

Table 2: Cities & Regencies Expenditure during Semester I-2020

Expenditure	Quadrant I	Quadrant II	Quadrant III	Quadrant IV
	Growth Average (yoy)	Growth Average (yoy)	Growth Average (yoy)	Growth Average (yoy)
Total of Expenditure	-11,55%	-11,07%	12,11%	13,98%
Social Aid Expenditure	148,66%	-22,63%	4,87%	51,40%
Grant Expenditure	248,37%	253,51%	190,42%	316,51%
Unexpected Expenditure	17,22%	53,34%	-13,80%	8,36%
Goods and Services Expenditure	-10,81%	-3,47%	2,71%	7,77%
Capital Expenditure	50,36%	-41,18%	98,37%	56,30%
Employee Expenditure	-9,79%	-16,20%	-5,09%	-1,72%

Source: Economic Research Division PT. SMI., 2020: 152-153

Regional financial capability during the Covid-19 Pandemic could be seen in the 4 (four) indicators as described aforementioned. The four indicators are (1) common condition of regional fiscal during the Covid-19 Pandemic, (2) the framework of regional fiscal mapping, (3) regional fiscal mapping during the Covid-19 Pandemic, and (4) the components of regional income.

DISCUSSION

Based on the presented data in the present research results, the reseacher explains the answers for the proposed two research questions in this discussion. The first research question is: how is the impact of regional financial capability during the Covid-19 Pandemic towards regional fiscal capacity? Based on the data gained in common condition of regional fiscal during Covid-19 Pandemic, in general the Covid-19 Pandemic decreased the provincial revenues and expenditures in almost all provinces in Indonesia in the first semester of 2020. However, several provinces, such as Banten, North Kalimantan, Papua, and West Sumatera increased in provincial revenues and expenditures.

Furthermore, based on the presented data in regional fiscal mapping during the Covid-19 Pandemic, in general, from the research sample of 66 regencies/cities, there were 30 regencies/cities located in quadrant I decreased in revenue and expenditure caused by the Covid-19 Pandemic. Furthermore, there were 19 regencies/cities located in quadrant III implemented a counter-cyclical policy through maintaining economic stability, decreasing revenues, and increasing local government expenditures. The reduction revenues from each region in quadrants I and III were caused by the reduction on regional taxes around 2,5 percent (yoy) and 10,68 percent (yoy) sequentially in the first semester of 2020, fiscal balance transfers around 8,42 percent (yoy), and general allocation grant (DAU) around 9,8 percent (yoy) and 6,94 percent (yoy) sequentially.

Afterwards, the second research question is: how are local governments' efforts to solve the impact of the Covid-19 Pandemic towards regional fiscal capacity? Based on the presented data in regional fiscal mapping during the Covid-19 Pandemic, there are 2 types of policies taken by regencies/cities. The first policy is to implement a counter-cyclical policy through maintaining economic stability, decreasing revenues, and increasing local government expenditures. Then, the second policy is to implement a pro-cyclical policy through increasing revenues and decreasing expenditures.

Meanwhile, regencies/cities that implemented a counter-cyclical policy generally increased in expenditure components, such as grant expenditures around 316,51 percent, and regional capital expenditures, which meant that some local governments could still build infrastructure (assets and buildings) during the Covid-19 Pandemic. However, local governments decreased around -1% - 16% for the employee expenditures.

Based on the aforementioned findings, the present research results are in harmony with the results of previous research such as Tan (2021). He (2021) stated that the impact of the Covid-19 Pandemic significantly influenced towards the reduction of regional fiscal capacity around 10% and the increase of regional expenditures around 5%. Thus, the Covid-19 Pandemic had threatened regional fiscal health which was proven by the reduction of realisation in the regional revenues, so that regional cash flows were obstructed and some regional priority expenditures were delayed. In addition, the Covid-19 Pandemic caused a current budget deficit in 2020. These were the national phenomena experienced by local governments in Indonesia during 2020.

CONCLUSIONS

The present research found that the Covid-19 Pandemic reduced regional revenue and expenditure in almost all provinces in Indonesia in the first semester of 2020. In general, from the research sample of 66 regencies/cities, 49 regencies/cities located in quadrant I and III decreased revenue caused by the Covid-19 Pandemic. The reduction revenues from each region in quadrants I and III were caused by the reduction on regional taxes around 2,5 percent (yoy) and 10,68 percent (yoy) sequentially in the first semester in 2020, fiscal balance transfers around 8,42 percent (yoy), and general allocation grant (DAU) around 9,8 percent (yoy) and 6,94 percent (yoy) sequentially.

To solve those above regional fiscal problems, the regional government implemented 2 types of policies. The first policy is to implement a counter-cyclical policy through maintaining economic stability, decreasing revenues, and increasing local government expenditures. Then, the second policy is to implement a pro-cyclical policy through increasing revenues and reducing expenditures. The present research also found that regencies/cities that implemented a counter-cyclical policy generally increased in expenditure components, such as grant expenditures around 316,51 percent, and regional capital expenditures, which meant that some local governments were still able to build infrastructure (assets and buildings) during the Covid-19 Pandemic. However, local governments decreased around -1% - 16% for the employee expenditures.

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