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Fiscal Decentralization Policy and Its Impact on the Development of Underdeveloped Regions in South Sulawesi

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ABSTRACT

Fiscal decentralization has been a key element of Indonesia's regional autonomy policy, aiming to distribute authority and resources from the central to local governments to foster equitable development. Despite substantial increases in fiscal transfers through mechanisms such as the General Allocation Fund (DAU) and Special Allocation Fund (DAK), underdeveloped regions in South Sulawesi continue to face persistent development gaps in infrastructure, public services, and socioeconomic outcomes. This study aims to examine the implementation of fiscal decentralization policies and their impact on the development of underdeveloped districts in South Sulawesi, focusing on the interplay between fiscal transfers, local governance capacity, and geographic constraints. Using a qualitative library research method, data were collected from government regulations, official reports, statistical data, and scholarly literature, and analyzed through content analysis to identify key themes related to policy objectives, implementation, and development outcomes. The findings reveal that while fund allocation and disbursement rates are generally high, the developmental impact is constrained by weak budget planning, limited technical capacity, poor inter-agency coordination, and the dominance of routine expenditures over capital investments. Geographic challenges, particularly in remote and island districts, further inflate development costs and delay project completion. The study concludes that fiscal decentralization in South Sulawesi requires comprehensive reform, including differentiated allocation formulas, performance-based incentives, enhanced technical assistance, and stronger accountability mechanisms. Such measures are essential to ensure that fiscal decentralization achieves its intended goal of promoting inclusive, equitable, and sustainable regional development.

Keyword: Fiscal Decentralization, Regional Development, Governance Capacity

INTRODUCTION

Fiscal decentralization has become one of the fundamental pillars of Indonesia's regional autonomy policy, designed to distribute authority and resources from the central government to local governments with the expectation of fostering equitable development (Smoke & Lewis, 1996; Talitha et al., 2020). Since the early 2000s, Indonesia has implemented a variety of fiscal transfer mechanisms such as the General Allocation Fund (DAU), Special Allocation Fund (DAK), Revenue Sharing Fund, and Village Fund intended to enable local governments to plan and execute development programs tailored to local needs

(Augustine et al., 2023; Suryantini, 2017). In theory, such fiscal transfers should accelerate progress in underdeveloped regions by allowing for context-specific solutions (Bird & Smart, 2002; Henkel et al., 2021). However, the persistent presence of significant interregional disparities, especially in provinces like South Sulawesi, raises questions about whether fiscal decentralization is functioning as an effective tool for reducing inequality.

Table 1. Fund Allocation for South Sulawesi in 2023

Fund Type	Budgeted (IDR)	Realized (IDR)	Realization Rate
DAU	2,340,040,525,000	2,340,040,525,000	100%
DAK (Physical)	321,993,568,000	277,662,200,635	86.23%
DAK (Non-Physical)	1,198,433,427,000	1,108,771,610,279	92.52%

Source: sulsel.prov.go.id, 2023

The urgency of addressing the problem lies in the persistent development disparities between advanced and underdeveloped districts in South Sulawesi despite consistent increases in fiscal transfers from the central government. In 2023 alone, the province received more than IDR 2.34 trillion in DAU and over IDR 1.5 trillion in combined DAK allocations, yet significant gaps remain in infrastructure availability, public service quality, and socioeconomic indicators (Haruni, 2023). The relatively high realization rates 100% for DAU, 92.52% for non-physical DAK, and 86.23% for physical DAK highlight that the problem is not simply one of fund disbursement, but rather of how effectively these funds are managed, targeted, and adapted to local geographic and institutional constraints. Without urgent reforms to improve governance capacity, policy targeting, and accountability, there is a real risk that fiscal decentralization will continue to perpetuate, rather than close, the inequality gap between South Sulawesi's thriving urban centers and its lagging peripheral regions (Kis-Katos & Sjahrir, 2017).

The academic discussion around fiscal decentralization often emphasizes its potential to enhance efficiency and responsiveness in public service delivery by placing decision-making closer to the community (Oates, 1999). Nevertheless, empirical evidence from Indonesia suggests that without adequate institutional capacity, fiscal autonomy can fail to translate into tangible development gains (Santi & Iskandar, 2021). In South Sulawesi, challenges such as limited budget planning expertise, weak inter-agency coordination, and insufficient public participation have constrained the ability of local governments to maximize the developmental impact of fiscal transfers. Additionally, the dominance of routine expenditure over capital investment has further hampered long-term growth prospects, especially in underdeveloped regions.

Geographical and logistical constraints exacerbate these challenges. South Sulawesi's diverse topography ranging from mountainous inland districts to remote islands complicates the equitable delivery of infrastructure and services (Astari et al., 2024). The cost of development projects in isolated areas like the Selayar Islands is substantially higher due to transportation difficulties and the scarcity of necessary resources. Such conditions not only strain local budgets but also limit the reach and sustainability of development initiatives. Without policy mechanisms that adequately account for these geographic realities, fiscal decentralization risks becoming a blunt instrument incapable of addressing localized barriers to development (Bird & Smart, 2002; Epple & Nechyba, 2004).

The contribution of this study lies in its critical examination of how fiscal decentralization interacts with local governance capacity, geographic constraints, and institutional accountability to shape development outcomes in underdeveloped regions (Maket & Naibei, 2025; Song et al., 2025; Zheng et al., 2025). Unlike prior studies that have treated fiscal transfers largely as a quantitative phenomenon, this article underscores the qualitative dimensions of governance and contextual adaptation in determining policy effectiveness

(Manga & Fouopi, 2025; Ren et al., 2025). The findings provide valuable insights for policymakers seeking to reformulate fiscal allocation mechanisms, strengthen local governance capacities, and design interventions that are both equitable and context-sensitive. Given the persistent disparities in South Sulawesi, this research demonstrates the importance of rethinking fiscal decentralization not merely as a matter of fund distribution but as a holistic governance reform aimed at achieving inclusive and sustainable development.

RESEARCH METHODS

This research employs a qualitative approach using the library research method to analyze (Coast & Jackson, 2017; Patton, 2002) the implementation of fiscal decentralization policies and their impact on the development of underdeveloped regions in South Sulawesi. The library research method is considered appropriate because it enables a deep theoretical and conceptual examination based on documented and verifiable sources. Data were collected from legislation such as Law No. 23 of 2014 on Regional Government and Ministry of Finance regulations on transfer funds official government reports, statistical data from the Central Statistics Agency (BPS), and scholarly literature discussing fiscal decentralization, interregional disparities, and local governance capacity.

The data collection process involved identifying and selecting credible sources published within the last two decades, prioritizing those with direct relevance to South Sulawesi's development context. Key sources included the 2022 Regional Development Performance Report of South Sulawesi Province by Bappelitbangda, fiscal transfer records, and journal articles offering both supportive and critical perspectives on the effectiveness of fiscal decentralization. This selection process ensured a balanced evidence base that incorporated legal frameworks, empirical statistics, and academic analysis.

For data analysis, the study applied content analysis to systematically categorize and interpret findings under three thematic areas: (1) the principles and objectives of fiscal decentralization, (2) the implementation of fiscal policies in underdeveloped regions, and (3) measurable development outcomes in South Sulawesi's lagging districts. Triangulation was conducted by cross-referencing government data with academic assessments to validate findings and minimize bias. This methodological approach enables the research to provide a comprehensive understanding of fiscal decentralization's practical impact and its implications for achieving inclusive and equitable regional development.

RESULTS AND DISCUSSION

1. Fiscal Allocation Patterns and Capacity Gaps

The analysis shows that although fiscal allocations such as the General Allocation Fund (DAU) and Special Allocation Fund (DAK) for South Sulawesi increase annually, their impact on accelerating development in underdeveloped regions remains limited. Districts such as North Luwu and Enrekang face persistent capacity gaps in budget planning and implementation due to a shortage of skilled human resources, weak coordination among agencies, and the absence of accurate spatial and sectoral data. This mismatch between available funds and institutional capacity often results in short-term or ceremonial projects that fail to address structural development issues.

Table 2. Deep Analysis of Fiscal Allocation Patterns and Capacity Gaps – South Sulawesi

Issue	Risk if Unaddressed	Action
Allocation growth vs outcome stagnation	Persistent inequality; inefficient spending; failure to meet development goals.	Reform allocation formulas to include geographic and cost indices; link part of DAU/DAK to measurable outputs; expand technical assistance.

Issue	Risk if Unaddressed	Action
Budget planning capacity shortfalls	Low value-for-money; recurring budget carry-overs; unmet targets.	Build professional planning cadre; require feasibility studies and complete designs; implement planning mentorship programs.
Inter-agency coordination & data limitations	Mis-targeted projects; duplication of efforts; slower poverty reduction.	Integrate fiscal–spatial dashboards; standardize sectoral data; institutionalize joint planning forums with binding decisions.
Spending quality imbalance (operations vs capital)	Infrastructure gaps persist; weak long-term growth; low investor confidence.	Protect capital expenditure minimums; implement early procurement; introduce multi-year budgeting and framework contracts.
Geographical cost differentials	Widening inequality in remote areas; systematic under-provision of services.	Add a geographic difficulty index to funding formulas; provide logistical support pools; schedule projects seasonally to avoid weather delays.
Weak accountability and participation	Reduced public trust; poor service alignment with community needs; potential misuse of funds.	Pilot participatory budgeting; strengthen inspectorate capacity; publish public dashboards tracking fund use and outcomes.

Source: Author, 2025

The table summarizes six key issues affecting the effectiveness of fiscal decentralization in South Sulawesi's underdeveloped regions during 2023. While fiscal allocations through the DAU and DAK have increased, their impact is hindered by structural and institutional challenges. One major problem is the mismatch between allocation growth and tangible development outcomes. Without more adaptive formulas that account for geographic difficulty and actual development needs, large transfers risk perpetuating existing inequalities. Similarly, gaps in budget planning capacity such as weak feasibility studies, limited technical skills, and poor project design result in short-term or low-impact projects, reducing the value-for-money of public spending.

Inter-agency coordination and data limitations further weaken policy execution. Inconsistent or incomplete sectoral data, minimal use of geospatial tools, and poor coordination among local planning bodies (Bappelitbangda and OPDs) contribute to mis-targeted projects and duplication of efforts. These issues are compounded by imbalances in spending composition, with operating expenditures crowding out capital investments essential for infrastructure and long-term growth. Additionally, South Sulawesi's diverse topography creates geographical cost differentials: remote and island districts face higher construction costs and frequent delays, which the current allocation mechanisms fail to adequately address.

Weak accountability and limited community participation complete the picture of systemic challenges. Although planning forums such as Musrenbang exist, they often function procedurally rather than substantively, with limited public influence on project selection. Oversight bodies, including inspectorates and local parliaments, often lack the resources and capacity to ensure proper fund utilization.

2. Low Quality of Regional Spending

Findings reveal that a significant portion of regional budgets in underdeveloped districts is absorbed by routine expenditures, primarily employee salaries, rather than capital investments in long-term growth sectors. For example, the Ministry of Finance (2022) reported that in some underdeveloped districts, capital expenditure accounted for less than 20% of total spending, far below the ideal ratio. This spending pattern has slowed the provision of essential infrastructure, such as roads, clean water networks, and public service facilities, thereby limiting the developmental impact of fiscal transfers.

Findings from the Ministry of Finance (2022) and supporting literature clearly indicate that the quality of regional spending in underdeveloped districts remains critically low. In many of these areas, such as North Luwu and Enrekang in South Sulawesi, the majority of local budgets are absorbed by routine expenditures, primarily employee salaries, rather than being allocated to capital investments aimed at long-term economic growth. This spending structure significantly undermines the potential developmental impact of fiscal transfers from the central government. In fact, the Ministry's evaluation shows that in several underdeveloped districts, the ratio of capital expenditure to total regional spending falls below 20%, a figure far from the ideal threshold for promoting sustained development. This imbalance reflects a structural problem in local fiscal management, where operational costs dominate at the expense of strategic development priorities.

The consequences of such spending patterns are evident in the slow progress of essential infrastructure development. Limited investment in capital projects has delayed the provision of basic facilities such as inter-regional road networks, clean water systems, and public service centers for education and healthcare. This infrastructure gap further constrains economic opportunities and limits access to vital services for local communities, particularly in geographically challenging regions such as the Selayar Islands and mountainous parts of East Luwu. The high logistical costs associated with these areas exacerbate the problem, as limited capital funds must also contend with inflated construction and transportation expenses. Consequently, even when projects are initiated, they often suffer from incomplete implementation or reduced scale due to budget constraints.

This situation reveals a deeper issue within the framework of Indonesia's fiscal decentralization policy: the availability of funds alone does not guarantee developmental progress without adequate local governance capacity. Weak institutional capabilities in budget planning, monitoring, and prioritization mean that even increasing nominal transfers cannot translate into significant development outcomes. Without a strategic shift towards a higher proportion of capital expenditure, combined with technical assistance, planning support, and stronger accountability mechanisms, underdeveloped districts will remain trapped in a cycle where fiscal resources sustain administrative operations rather than drive transformative growth. Addressing this imbalance is therefore essential to ensuring that fiscal transfers fulfill their intended role of reducing interregional disparities and promoting inclusive, long-term development.

3. Geographic and Logistical Constraints

South Sulawesi's geographic diversity poses substantial challenges to equitable development, with its landscape encompassing mountainous regions, coastal areas, and isolated islands. This varied topography not only complicates physical access but also significantly increases the cost and complexity of infrastructure projects. For instance, in the Selayar Islands, the per-unit cost of constructing public facilities is considerably higher than in mainland areas due to the need for specialized transport and the limited availability of construction materials. These higher costs often strain local budgets, especially in underdeveloped districts where fiscal capacity is already limited, resulting in fewer projects being initiated or completed compared to more accessible regions.

The logistical constraints extend beyond cost to the very feasibility of implementing development programs. Remote areas such as East Luwu and South Sinjai frequently experience delays in the delivery of materials, machinery, and skilled labor, particularly during the rainy season when road access is further limited. In these regions, transporting heavy equipment for road building, water supply systems, or health facilities can take weeks longer than in better-connected districts, delaying not only construction timelines but also the provision of essential services to local populations. Such delays can undermine public trust in government initiatives and contribute to a cycle of underdevelopment, where communities remain underserved despite the allocation of fiscal resources.

These geographic and logistical barriers also exacerbate inequality within the province, as areas with favorable accessibility are able to implement and benefit from development programs more rapidly. Without tailored fiscal and logistical strategies—such as adjusting transfer fund formulas to account for higher construction cost indices and implementing targeted infrastructure support remote and difficult-to-reach districts will continue to lag behind. Addressing these challenges requires a policy approach that goes beyond uniform funding allocations and instead integrates geographic realities into planning, resource distribution, and project management, ensuring that development efforts reach all communities regardless of their location.

4. Weak Accountability and Limited Public Participation

In many underdeveloped districts, public participation in development planning remains largely symbolic rather than substantive. Although formal mechanisms such as the Musrenbang (Regional Development Planning Forum) are in place to gather community input, these forums often fail to reflect the genuine priorities of local residents. Low fiscal literacy among community members, combined with the dominance of local elites in decision-making, results in planning processes that are top-down in nature. As a consequence, budget allocations may prioritize politically advantageous projects over those that address pressing community needs, further weakening the developmental impact of fiscal transfers.

Oversight institutions, including local parliaments (DPRD) and inspectorates, face their own challenges in ensuring fiscal accountability. Limited technical expertise, insufficient staffing, and a lack of independence hinder their capacity to conduct thorough reviews of budget proposals and monitor project implementation. In some cases, weak coordination between oversight bodies and civil society organizations reduces opportunities for external checks and balances. This lack of rigorous scrutiny increases the risk of inefficiency, misallocation of funds, and even corruption, particularly in regions where governance systems are already fragile.

Without significant improvements in both accountability mechanisms and public engagement, fiscal decentralization risks perpetuating existing disparities rather than narrowing them. Strengthening these elements requires a two-pronged approach: first, enhancing the technical capacity of oversight institutions to ensure transparent and effective budget management; and second, empowering communities through fiscal education and participatory governance programs. Such measures would not only improve the targeting and impact of development spending but also foster a culture of shared responsibility, ultimately making fiscal decentralization a more effective tool for promoting equitable growth.

Table 3. Analysis of Weak Accountability and Limited Public Participation in Fiscal Decentralization

Aspect	Key Points
Issues	• Symbolic public participation in Musrenbang • Weak fiscal accountability • Low capacity of oversight bodies
Causes	• Low fiscal literacy • Elite dominance in decision-making • Poor reflection of community needs • Limited skills, staffing, and independence in oversight bodies • Weak coordination with civil society
Impacts	• Top-down planning

Aspect	Key Points
	• Politically driven budget allocation • Risk of inefficiency, misallocation, corruption • Persistent regional disparities
Solutions	• Oversight capacity: training, staffing, independence • Community empowerment: fiscal education, participatory governance • Coordination: stronger links between oversight bodies and civil society
Goal	• Transparent, effective budgeting • Needs-based spending • Shared responsibility culture • Equitable growth through fiscal decentralization

Source: Author, 2025

The table provides a structured analysis of the challenges, causes, impacts, and potential solutions related to weak accountability and limited public participation in fiscal decentralization. It highlights how development planning forums such as Musrenbang often fail to genuinely represent community needs due to low fiscal literacy and the dominance of local elites. These factors, combined with the limited capacity and independence of oversight institutions, create a governance environment where political interests often take precedence over urgent community priorities. Weak coordination between oversight bodies and civil society further reduces the effectiveness of external checks and balances, leaving significant room for inefficiency, misallocation of funds, and even corruption.

The proposed solutions emphasize a three-pronged approach: strengthening the technical and institutional capacity of oversight bodies, empowering communities through fiscal education and participatory governance, and improving collaboration between oversight institutions and civil society organizations. By implementing these measures, fiscal decentralization can shift from a top-down, politically driven process to a transparent, needs-based system that fosters shared responsibility. Ultimately, these improvements aim to ensure that budget allocations are more targeted, effective, and equitable, thereby narrowing regional disparities and enhancing the overall developmental impact of fiscal transfers.

5. Need for Reformulation of Fiscal Decentralization Policy Design

The persistent challenges observed in underdeveloped districts underscore the urgent need for a reformulation of Indonesia's fiscal decentralization policy design. Current transfer mechanisms, such as the General Allocation Fund (DAU) and Special Allocation Fund (DAK), rely heavily on formula-based allocations that treat regions in a uniform manner, often overlooking critical factors like geographic isolation, infrastructure deficits, and disparities in local governance capacity. This "one-size-fits-all" approach fails to account for the higher construction costs in remote areas, the additional logistical burdens of serving island communities, and the limited administrative capacity in districts with weak institutional frameworks. As a result, fiscal transfers frequently sustain operational expenditures without generating the transformative impact required to close development gaps.

A more responsive policy framework would incorporate differentiated allocation formulas that take into account the unique challenges of each region. This could include variables such as a Construction Cost Index, a Geographic Difficulty Index, and measures of local fiscal capacity to ensure that regions facing higher barriers receive proportionally greater support. In parallel, fiscal transfers should be linked not only to the quantity of funding provided but also to qualitative improvements in governance and budget transparency. For example, performance-based incentives, such as the Regional Incentive Fund (Dana Insentif

Daerah/DID), could be redirected towards underdeveloped districts that demonstrate progress in public accountability, effective budget utilization, and measurable improvements in service delivery.

Reform efforts must also go beyond funding formulas to include targeted technical assistance, capacity-building programs, and stronger oversight mechanisms. Providing local governments with planning support, data management tools, and training in financial management would enhance their ability to design and implement high-impact development projects. At the same time, regular monitoring and evaluation from the central government, combined with active public participation at the community level, would help ensure that fiscal resources are used efficiently and equitably. Without such a comprehensive recalibration of policy design, fiscal decentralization will continue to fall short of its potential as an engine for inclusive and sustainable regional development.

CONCLUSION

The study concludes that while fiscal decentralization in Indonesia, particularly in South Sulawesi, has succeeded in increasing the flow of funds to underdeveloped regions, its impact on reducing interregional disparities remains limited. Persistent challenges such as weak institutional capacity, inadequate budget planning, and poor coordination among local agencies hinder the effective utilization of fiscal transfers. Additionally, the current allocation formulas do not sufficiently account for geographic and logistical complexities, resulting in underfunded and delayed projects in remote areas. Without addressing these structural weaknesses, fiscal decentralization risks reinforcing existing inequalities rather than bridging them.

Moreover, the research highlights that a disproportionate share of regional budgets in underdeveloped districts is absorbed by routine expenditures instead of capital investments that drive long-term growth. This imbalance significantly restricts the development of essential infrastructure and public services, particularly in geographically challenging areas like mountainous districts and isolated islands. The lack of targeted investment exacerbates socioeconomic disparities and limits the potential for sustainable development. Accountability mechanisms and public participation, though formally present, often function more as procedural requirements than as effective tools for ensuring responsive and transparent governance.

Given these findings, the study recommends a comprehensive reformulation of fiscal decentralization policy. This includes revising allocation formulas to reflect regional cost differentials, linking transfers to governance performance, and expanding technical assistance to local governments. Strengthening institutional capacity, improving data quality, and fostering genuine community participation are essential to ensuring that fiscal decentralization fulfills its intended role of promoting equitable, inclusive, and sustainable development across South Sulawesi. Without such reforms, the promise of fiscal decentralization as a driver of balanced regional growth will remain unfulfilled.

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