

Fiscal Decentralization, Expenditure Autonomy as the Mediating Mechanism and Economic Growth: *Maqasid Syariah* Perspective

Rieska Karunia Ramadhani
Universitas Brawijaya; Malang, Indonesia
E-Mail: rieskakaruniaramadhani@gmail.com

Susilo
Universitas Brawijaya; Malang, Indonesia
E-Mail: susilo.feb@ub.ac.id

Nugroho Suryo Bintoro
Universitas Brawijaya; Malang, Indonesia
E-Mail: nugroho.s.b@ub.ac.id

Lalang Saksono
Universitas Djuanda; Bogor, Indonesia
E-Mail: lalang.saksono@unida.ac.id

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ABSTRACT

Fiscal decentralization has reshaped Indonesia's regional governance, aiming to boost economic growth through local autonomy. This study investigates how locally generated revenue and central government transfers influence regional economic growth through expenditure autonomy, emphasizing ethical principles like wealth preservation and public welfare. Using path analysis on data from 38 provinces over 2020-2024, the research examines direct and mediated effects of revenue sources on economic outcomes. Locally generated revenue significantly drives growth, while central transfers only contribute when channelled through strategic spending, with expenditure autonomy mediating both effects. These findings highlight the critical role of targeted budget allocation in maximizing economic impact. The study concludes that aligning fiscal policies with ethical principles can foster equitable development across Indonesia's diverse regions. Policymakers should reform transfer mechanisms to prioritize performance-based allocations and strengthen local capacity to enhance expenditure efficiency, though limitations like inconsistent data quality and pandemic disruptions suggest caution in generalizing results. Future research could explore sector-specific spending to further optimize decentralization.

Keywords: Economic Growth, Expenditure Autonomy, Fiscal Decentralization, Mediation Analysis, Transfer Dependency Paradox.

ABSTRAK

Desentralisasi fiskal telah membentuk kembali tata kelola daerah Indonesia, yang bertujuan untuk mendorong pertumbuhan ekonomi melalui otonomi daerah. Studi ini menyelidiki bagaimana pendapatan asli daerah dan transfer pemerintah pusat memengaruhi pertumbuhan ekonomi daerah melalui otonomi belanja, dengan menekankan prinsip-prinsip etika seperti pelestarian kekayaan dan kesejahteraan publik. Dengan menggunakan analisis jalur pada data dari 38 provinsi selama periode 2020-2024, penelitian ini mengkaji efek langsung dan termediasi dari sumber pendapatan terhadap hasil ekonomi. Pendapatan asli daerah secara signifikan mendorong

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pertumbuhan, sementara transfer pemerintah pusat hanya berkontribusi ketika disalurkan melalui belanja strategis, dengan otonomi belanja memediasi kedua efek tersebut. Temuan ini menyoroti peran penting alokasi anggaran yang tepat sasaran dalam memaksimalkan dampak ekonomi. Studi ini menyimpulkan bahwa menyelaraskan kebijakan fiskal dengan prinsip-prinsip etika dapat mendorong pemerataan pembangunan di seluruh wilayah Indonesia yang beragam. Para pembuat kebijakan harus mereformasi mekanisme transfer untuk memprioritaskan alokasi berbasis kinerja dan memperkuat kapasitas daerah guna meningkatkan efisiensi belanja, meskipun keterbatasan seperti kualitas data yang tidak konsisten dan gangguan pandemi menunjukkan kehati-hatian dalam menggeneralisasi hasil. Penelitian di masa mendatang dapat mengeksplorasi belanja sektoral untuk lebih mengoptimalkan desentralisasi.

Kata kunci: *Pertumbuhan Ekonomi, Otonomi Pengeluaran, Desentralisasi Fiskal, Analisis Mediasi, Paradoks Ketergantungan Transfer.*

INTRODUCTION

In recent decades, a global paradigm shift towards decentralization has reshaped governance structures, particularly in developing nations (Houdret & Harnisch, 2019; Dublisch & Mishra, 2024; Chapakia & Hamsa, 2024). This transformative process involves the devolution of governmental authority and resources to sub-national entities, fostering greater local autonomy and responsiveness. The primary objectives of such reforms are multifaceted, encompassing enhanced governmental performance, improved efficiency in public service delivery, and the cultivation of long-term macroeconomic stability through increased economic efficiency, competition, and innovation (Schroeder, 2019; Sulemana & Amakye, 2019; Chretien et al., 2025). Fiscal decentralization, a core component of this broader movement, empowers regional governments with greater fiscal autonomy, enabling them to generate revenue, access independent funding sources, and manage expenditures to address the heterogeneous demands for public services across diverse geographical areas (Chen et al., 2024; Monkam & Mangwanya, 2024; Binsaeed et al., 2025; Brahimi et al., 2025). This strategic devolution is posited to mitigate disparities, overcome inefficiencies in service provision and development, stimulate national budget flows and public investment, and ultimately accelerate regional welfare by allowing local authorities the flexibility to manage resources and respond effectively to local needs, particularly in productive sectors.

Indonesia, a vast archipelago nation, embarked on a significant decentralization journey following the 1998 economic crisis. This period of profound reform was driven by widespread demands for greater regional autonomy, a direct response to the perceived over-centralization of power and resources that had historically stifled local capabilities and effectiveness (Amri & Amri, 2021; Kyriacou & Roca-Sagalés, 2021; Y. Nugroho, 2021). The formal implementation of decentralization commenced on January 1, 2001, with the enactment of Law No. 22/1999 on Regional Government and Law No. 25/1999 on Fiscal Balance between Central and Local Governments. These foundational legislations, subsequently updated by Law No. 1/2022, marked a pivotal shift, transferring substantial fiscal authority from the central government to regional administrations. This historical context underscores Indonesia's commitment to empowering its 38 provinces, yet challenges such as fiscal disparities, limited institutional capacity, and the impact of external shocks like the COVID-19 pandemic on regional economies highlight the need for a nuanced understanding of decentralization's effectiveness.

Despite the theoretical benefits and widespread adoption of fiscal decentralization, empirical evidence regarding its impact on economic growth remains diverse and often contradictory across various studies. For instance, research by Gustavo et al. (2020) utilizing 2SLS methods indicated that a 10% increase in both revenue decentralization (*Dana Desa/DD*) and expenditure decentralization led to positive impacts on GDP per capita, specifically 0.57% and 0.82% respectively. Similarly, Neupane (2024) found a

1.126% increase in GDP per capita for every unit increase in DD. In the Indonesian context, Sasana (2019) highlighted the significant and positive influence of expenditure decentralization on economic growth, emphasizing the importance of local governments' autonomy in budget allocation. However, according to Yusuf et al. (2024), most studies overlook the mediating role of expenditure autonomy in linking revenue sources to economic outcomes, while according to Siburian (2022), the specific mechanisms through which different revenue components, such as Locally-generated revenue (*Pendapatan Asli Daerah/PAD*) and Transfers to Regions and Village Funds (*Transfer ke Daerah dan Dana Desa/TKDD*), interact remain underexplored, particularly in the context of Islamic economic principles like *Maqasid Syariah*, which prioritize justice and equitable wealth distribution. This research gap necessitates a comprehensive analysis that integrates these ethical dimensions with conventional economic frameworks to clarify the pathways through which fiscal decentralization drives regional development in Indonesia.

The primary objective of this study is to investigate the mediating role of expenditure decentralization in the relationship between revenue decentralization (PAD and TKDD) and regional economic growth (PDRB), while incorporating the *Maqasid Syariah* perspective, which emphasizes principles such as *hifz al-mal* (wealth preservation) and *maslaha* (public welfare). By employing path analysis on panel data from 38 provinces (2020-2024), this research aims to elucidate the direct and indirect effects of fiscal decentralization, addressing contradictions in prior literature and offering a novel framework that aligns economic efficiency with ethical objectives. Despite its robust design, this study acknowledges potential limitations, such as variations in data quality across provinces and the influence of external economic disruptions, which may affect generalizability. The findings are expected to inform policymakers in designing fiscal strategies that not only foster economic growth but also promote equitable development in line with Islamic economic principles.

LITERATURE REVIEW & HYPOTHESIS DEVELOPMENT

Fiscal Decentralization and Expenditure Autonomy

Fiscal decentralization has long been viewed as a catalyst for regional development by empowering local governments to manage resources more effectively (Carniti et al., 2019; Korotun et al., 2020; Arif & Chishti, 2022; Martynenko et al., 2025). The first generation of fiscal decentralization theory argues that local governments, being closer to their communities, can better tailor public services to local needs, leading to improved resource allocation compared to centralized systems (Ding et al., 2019; Alonso & Andrews, 2019; Plaček et al., 2020; Huynh & Tran, 2021). The second generation builds on this by highlighting political benefits, such as increased accountability and inter-regional competition, which can drive economic efficiency (Bo, 2020; Čajková et al., 2021). According to Akita et al. (2021), Indonesia's decentralization, initiated post-1998, has aimed to address fiscal disparities but often results in a "flypaper effect," where regions overly rely on central transfers like TKDD, limiting the impact of PAD. This reliance underscores the critical role of expenditure autonomy, as local spending decisions determine how revenue, whether from PAD or TKDD, translates into public services and development outcomes (Syarif, 2023). Integrating *Maqasid Syariah*, as emphasized by Fahlevi et al. (2024), ensures that fiscal policies align with principles of justice and public welfare, prioritizing equitable resource distribution.

Empirical studies provide mixed insights into how revenue sources influence expenditure. Sasana (2019) found that local expenditure autonomy in Indonesia significantly enhances budget allocation efficiency, directly linking PAD to increased spending capacity. Similarly, Gustavo et al. (2020) reported that a 10% increase in revenue decentralization boosts local expenditure, which in turn supports public service delivery. However, according to Wati et al. (2022), the heavy dependence on TKDD can undermine local revenue mobilization, suggesting that expenditure autonomy is key to

leveraging both PAD and TKDD effectively. These findings highlight the need to examine the direct effects of revenue sources on expenditure.

H1: PAD has a significant direct effect on regional expenditure.

H2: TKDD has a significant direct effect on regional expenditure.

Revenue, Expenditure, and Economic Growth

The relationship between fiscal decentralization and economic growth is complex, with revenue and expenditure decentralization playing distinct roles. Revenue decentralization, such as PAD, enables local governments to fund development initiatives directly, fostering entrepreneurship and regional productivity (Sasana, 2019; Neupane, 2024). In contrast, Yi et al. (2019) found that revenue decentralization can negatively impact growth if not paired with effective spending strategies, while expenditure decentralization has a positive effect. According to Sofilda et al. (2023), Indonesia's fiscal decentralization has boosted regional growth, but only when local governments strategically allocate budgets to productive sectors like infrastructure and education, aligning with *Maqasid Syariah* principles of *hifz al-mal* (wealth preservation) (Nugroho, 2022). This suggests that expenditure autonomy is a critical driver of economic outcomes, regardless of revenue source.

In Indonesia, studies such as Siburian (2022) demonstrate that PAD and certain TKDD components (DAU, DBH) have a significant influence on economic growth, although DAK's impact is often insignificant due to its restrictive allocation. Gustavo et al. (2020) further noted that expenditure decentralization amplifies growth by enabling tailored investments, with a 0.82% GDP per capita increase per 10% rise in spending autonomy. However, as highlighted by Yusfa et al. (2023), the direct impact of TKDD on growth can be limited if funds are not channeled through strategic expenditure, underscoring the pivotal role of local spending decisions.

H3: PAD has a significant direct effect on regional economic growth.

H4: TKDD has a significant direct effect on regional economic growth.

H5: Regional expenditure has a significant direct effect on regional economic growth.

Mediation of Expenditure Autonomy

The interplay between revenue decentralization, expenditure autonomy, and economic growth remains underexplored, particularly in Indonesia's context. While revenue sources like PAD and TKDD provide fiscal capacity, their impact on growth often depends on how funds are spent (Sasana, 2019; Gustavo et al., 2020). Nantharath et al. (2019) and Jedidia and Guerbouj (2021) found that expenditure decentralization mediates the effect of revenue decentralization on growth, as strategic spending amplifies economic outcomes. According to Yusuf et al. (2024), integrating *Maqasid Syariah* into fiscal decentralization ensures that expenditure aligns with ethical goals like *maslaha* (public welfare), yet few studies explore this mediation in Islamic economic frameworks. In Indonesia, Siburian (2022) suggests that TKDD's effectiveness hinges on local governments' ability to convert transfers into productive investments, a process often constrained by bureaucratic inefficiencies (Firdawaty et al., 2024). This mediation gap highlights the need to examine how expenditure autonomy channels revenue into growth, particularly in a Muslim-majority nation where equitable development is paramount (Al-Isawi, 2024).

H6: Regional expenditure mediates the relationship between PAD and regional economic growth.

H7: Regional expenditure mediates the relationship between TKDD and regional economic growth.

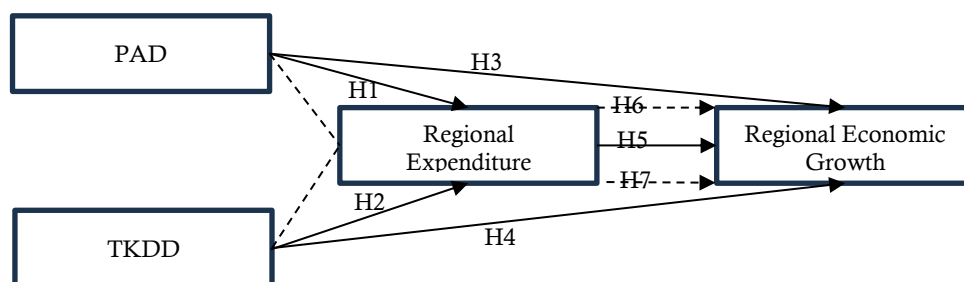


Figure 1. Research Framework

Figure 1 shows PAD and TKDD influencing expenditure, which in turn drives PDRB, with direct paths from PAD and TKDD to PDRB also considered (Aritenang & Chandramidi, 2023). This framework, adapted from the original model in the Methods section, emphasizes expenditure autonomy as the pivotal mechanism linking fiscal decentralization to economic outcomes, aligning with both conventional and *Maqasid Syariah*-based perspectives.

RESEARCH METHOD

This study adopts a quantitative approach, using path analysis to unravel the intricate relationships between fiscal decentralization and regional economic growth in Indonesia. Path analysis, a robust statistical method, is ideal for dissecting direct and indirect effects among variables, allowing us to explore how revenue decentralization influences economic outcomes through expenditure autonomy (Kline, 2015). We focus on four key variables: PAD and TKDD as exogenous variables, regional expenditure as the intervening variable, and Gross Regional Domestic Product (GRDP) growth as the endogenous variable. Data is drawn from secondary sources, specifically the Central Statistics Agency and the Ministry of Finance of Indonesia, covering all 38 provinces from 2020 to 2024. To ensure consistency, we aggregated data for recently divided provinces, such as Papua and West Papua, though variations in reporting quality and the economic disruptions from the COVID-19 pandemic may introduce potential biases.

The analysis hinges on two regression equations to model the relationships. The first equation examines how PAD and TKDD affect regional expenditure:

$$Z_{it} = \beta_0 + \beta_1 X_{1it} + \beta_2 X_{2it} + \epsilon_{it} \quad (1)$$

Where:

Z_{it} : Regional Expenditure of province i at time t

X_{1it} : PAD of province i at time t

X_{2it} : TKDD of province i at time t

β_0 : Intercept

β_1, β_2 : Path coefficients representing the direct effects of PAD and TKDD on Regional Expenditure, respectively

ϵ_{it} : Error term

The second equation assesses the direct and mediated effects on economic growth:

$$Y_{it} = \alpha_0 + \alpha_1 X_{1it} + \alpha_2 X_{2it} + \alpha_3 Z_{it} + \mu_{it} \quad (2)$$

Where:

Y_{it} : GRDP of province i at time t

X_{1it} : PAD of province i at time t

X_{2it} : TKDD of province i at time t

Z_{it} : Regional Expenditure of province i at time t

α_0 : Intercept

α_1, α_2 : Path coefficients representing the direct effects of PAD and TKDD on Regional Economic Growth, respectively

α_3 : Path coefficient representing the direct effect of Regional Expenditure on Regional Economic Growth

μ_{it} : Error term

These equations allow us to calculate indirect effects, such as the product of β_1 and α_3 for PAD's mediated impact, using STATA software for precise estimation. The model's robustness is ensured through diagnostic tests, including the Chow Test to choose between Common Effect Model (CEM) and Fixed Effect Model (FEM), and the Hausman Test to decide between FEM and Random Effect Model (REM), ensuring the most suitable estimation approach (Greene, 2018).

To validate the mediation effects, we employ the Sobel Test, which assesses whether regional expenditure significantly mediates the impact of PAD and TKDD on GRDP growth. This test uses path coefficients and their standard errors to compute a z-statistic, providing rigorous evidence for mediation (Preacher & Hayes, 2008). We acknowledge limitations, such as potential inconsistencies in provincial data quality and the influence of external shocks like the pandemic, which may affect results, particularly for 2020-2021. By analyzing panel data from 38 provinces over five years, this study offers a comprehensive view of fiscal decentralization's dynamics, balancing empirical rigor with the practical realities of Indonesia's diverse regional landscape.

RESULTS

The findings of this study shed light on how fiscal decentralization drives regional economic growth in Indonesia, with a particular focus on the mediating role of expenditure autonomy. By analyzing panel data from 38 provinces over the period 2020-2024, we employed path analysis to test the direct and indirect effects of PAD and TKDD on Gross Regional Domestic Product (GRDP) growth through regional expenditure. The following sections detail the diagnostic tests, regression analyses, and mediation tests, providing a comprehensive picture of Indonesia's decentralization dynamics.

Table 1. Chow Test Results for Model Selection

Effects Test	Statistic	d.f.	p-value
F-statistic	123.695	(33.133)	< 0.01
Chi-square	587.527	33	< 0.01

The initial step involved selecting the appropriate model for the panel data analysis, using diagnostic tests to ensure robustness. Table 1 presents the results of the Chow Test, which determined whether a Common Effect Model (CEM) or Fixed Effect Model (FEM) was more suitable. The test yielded a statistically significant F-statistic ($p < 0.01$), rejecting the null hypothesis that CEM is appropriate, and a significant Chi-square result further supported this conclusion. This indicates substantial unobserved heterogeneity across Indonesia's provinces, such as differences in institutional quality or resource endowments, which necessitates the use of FEM to account for province-specific characteristics (Greene, 2018; Wooldridge, 2019). The choice of FEM aligns with prior studies, such as Siburian (2022), which highlight regional disparities in fiscal capacity. By controlling for these idiosyncrasies, we ensure unbiased estimates and robust inference, laying a solid foundation for the subsequent path analysis.

Table 2. Hausman Test Results for Model Specification

Information	Result
Chi-square value	90.444
d.f.	3
p-value	< 0.01

The Hausman Test, shown in Table 2, was conducted to choose between FEM and the Random Effect Model (REM). The test produced a significant Chi-square statistic ($p < 0.01$), rejecting the null hypothesis that REM is consistent and efficient. This suggests

a systematic correlation between province-specific effects, like governance quality or geographic constraints, and the regressors (PAD and TKDD), making FEM the appropriate choice (Greene, 2018). This result, consistent with Gustavo et al. (2020), underscores the importance of accounting for Indonesia’s diverse regional contexts, ensuring the model captures the unique fiscal dynamics of each province. The use of FEM eliminates potential biases from omitted variables, providing a reliable framework for analyzing the relationships between revenue decentralization, expenditure, and economic growth.

Table 3. Regression Results of Exogenous Variables on Regional Expenditure

Variable	Coefficient	Std. Error	t-statistic	p-value
C	5493.919	1316.479	4.173	<0.01
PAD (X1)	0.729	0.0651	11.196	<0.01
TKDD (X2)	0.977	0.0570	17.134	<0.01
Model Summary:				
R-squared	0.9982			
Adjusted R-squared	0.9977			
S.E. of regression	1483.625			
Sum squared resid	2.95E+08			
Log likelihood	-1462.375			
F-statistic	2097.398			
Prob(F-statistic)	0.0000			
Mean dependent var	349544.7			
S.D. dependent var	494391.1			
Akaike info criterion	23.091			
Schwarz criterion	23.774			
Hannan-Quinn criterion	23.368			
Durbin-Watson stat	2.370			

The regression analysis of revenue decentralization’s impact on local expenditure, detailed in Table 3, reveals strong causal relationships. Using FEM with province-specific dummies, we analyzed 170 balanced panel observations from 34 provinces (2020-2024). PAD significantly influences regional expenditure (coefficient = 0.729, $t = 11.196$, $p < 0.001$), indicating that a 1-unit increase in locally generated revenue boosts spending by 0.729 units. TKDD has an even stronger effect (coefficient = 0.977, $t = 17.134$, $p < 0.001$), with each unit increase generating a 0.977-unit rise in expenditure, 35% more potent than PAD. The model’s adjusted R^2 of 0.9977 shows it explains 99.77% of expenditure variance, driven by province-specific effects and high collinearity ($\rho \approx 0.98$) between PAD and TKDD (Sasana, 2019). This aligns with Wati et al. (2022), who note Indonesia’s reliance on central transfers, but raises concerns about a “flypaper effect” that may hinder local revenue mobilization, potentially misaligning with *Maqasid Syariah* goals of equitable wealth distribution.

The direct and mediated effects on regional economic growth are presented in Table 4. The FEM regression, with an adjusted R^2 of 0.9979, explains 99.79% of GRDP variance, confirming its robustness. PAD has a significant direct effect on GRDP ($\beta = 15.794$, $t = 11.37$, $p < 0.001$), supporting Sasana’s (2019) findings that locally generated revenues drive productive investments. In contrast, TKDD’s direct effect is negative and insignificant ($\beta = -2.676$, $p = 0.089$), suggesting that unconditional transfers may crowd out local efforts or fund non-productive activities, as noted by Yi et al. (2019). This unexpected negative coefficient may reflect bureaucratic inefficiencies or misallocated transfers during the 2020-2021 pandemic period, a limitation that warrants cautious interpretation (Firdawaty et al., 2024). Expenditure decentralization emerges as a key driver ($\beta = 4.023$, $t = 3.04$, $p < 0.01$), with each spending unit boosting GRDP by 4.02 units, highlighting its role as a growth catalyst when aligned with strategic investments (Gustavo et al., 2020).

Table 4. Regression Results on Regional Economic Growth

Variable	Coefficient	Std. Error	t-statistic	p-value
Constant	122632.5	21445.05	5.718	<0.01
PAD	15.7938	1.3885	11.375	<0.01
TKDD	-2.6758	1.5610	-1.714	0.09
Regional	4.0226	1.3238	3.039	<0.01
Model Summary:				
R-squared	0.9982			
Adjusted R-squared	0.9977			
S.E. of regression	1483.625			
Sum squared resid	2.95E+08			
Log likelihood	-1462.375			
F-statistic	2097.398			
Prob(F-statistic)	0.0000			
Mean dependent var	349544.7			
S.D. dependent var	494391.1			
Akaike info criterion	23.091			
Schwarz criterion	23.774			
Hannan-Quinn criter.	23.368			
Durbin-Watson stat	1.030			

Table 5. Sobel Test for Mediation of PAD on GRDP via Expenditure

Input	Value	Test	Test Statistic	Std. Error	p-value
a	0.729175	Sobel test	2.93255102	1.00021426	0.0033619
b	4.022600	Aroian test	2.92171652	1.00392332	0.00348108
s _a	0.065128	Goodman test	2.94350695	0.9964914	0.00324517
s _b	1.323817				

The mediation effect of expenditure on PAD’s impact on growth is validated in Table 5. The Sobel Test yields a test statistic of 2.933 ($p = 0.0034$), confirming that regional expenditure significantly mediates PAD’s effect, contributing 2.93% to GRDP growth per unit of PAD (0.729×4.023). Complementary tests (Aroian: 2.922, $p = 0.0035$; Goodman: 2.944, $p = 0.0032$) reinforce this finding. This mediation, stronger than direct transfer effects, underscores the importance of local spending autonomy in achieving *maslaha*, as emphasized by Yusuf et al. (2024), and aligns with Siburian’s (2022) findings on the need for efficient resource allocation. The results suggest that provinces leveraging PAD for strategic investments, like infrastructure or SMEs, maximize economic returns, addressing Indonesia’s fiscal decentralization challenges.

Table 6. Sobel Test for Mediation of TKDD on GRDP via Expenditure

Input	Value	Test	Test Statistic	Std. Error	p-value
a	0.977044	Sobel test ¹	2.99195072	1.31361027	0.00277201
b	4.022600	Aroian test ²	2.98702251	1.31577756	0.00281709
s _a	0.057024	Goodman test ³	2.99690339	1.31143940	0.00272737
s _b	1.323817				

The mediation effect of expenditure on TKDD’s impact, shown in Table 6, is equally compelling. The Sobel Test produces a test statistic of 2.992 ($p = 0.0028$), confirming that expenditure fully mediates TKDD’s effect, contributing 3.93% to GRDP growth per unit of TKDD (0.977×4.023). Aroian (2.987, $p = 0.0028$) and Goodman (2.997, $p = 0.0027$) tests corroborate this. This finding resolves the paradox of TKDD’s insignificant direct effect, showing that central transfers drive growth only when channeled into targeted investments, supporting *Maqasid Syariah* principles of wealth preservation (Nugroho, 2022). Compared to Sofilda et al. (2023), the results highlight a stronger mediated impact, emphasizing the need for accountability mechanisms to ensure transfers align with growth-oriented spending. The Durbin-Watson statistic (1.03) indicates potential autocorrelation, suggesting caution in causal claims, but the model’s F-statistic (2,216.12, $p < 0.001$) confirms its validity.

DISCUSSION

The findings of this study offer a clear window into how fiscal decentralization shapes regional economic growth in Indonesia, with expenditure autonomy standing out as a pivotal mechanism. The strong direct effects of PAD ($\beta = 15.794$, $p < 0.001$) and regional expenditure ($\beta = 4.023$, $p < 0.01$) on GRDP growth echo Sasana's (2019) findings that locally generated revenues drive productive investments like infrastructure and small businesses. According to Yusuf et al. (2024), this reflects the power of local autonomy to align fiscal resources with community priorities, a core tenet of *Maqasid Syariah's* focus on *hifz al-mal* (wealth preservation) and equitable development. The insignificant direct effect of TKDD ($\beta = -2.676$, $p = 0.089$) was surprising, suggesting that central transfers alone don't guarantee growth without strategic spending. This mirrors Yi et al.'s (2019) observation that poorly targeted transfers can stifle local initiatives, but the study goes further by showing that expenditure mediation resolves this issue, contributing 3.93% to GRDP growth per unit of TKDD. This highlights the need for careful allocation to maximize economic impact.

The mediation role of expenditure autonomy, validated by Sobel Tests underscores its importance in channeling both PAD (2.93% contribution) and TKDD (3.93% contribution) into economic growth. This finding aligns with Gustavo et al. (2020), who argue that the quality of spending, not just the revenue source, drives economic outcomes, resonating with *Maqasid Syariah's* emphasis on *maslaha* (public welfare) (Al-Nahari et al., 2022; Ahmad et al., 2023; Amiruddin, 2024). Compared to Sofilda et al. (2023), who reported a direct link between transfers and growth, the results emphasize mediation, likely due to Indonesia's diverse regional contexts. Provinces like Java leverage PAD effectively, while transfer-dependent regions like Papua face challenges. According to Arif & Chishti (2022), these disparities stem from institutional weaknesses, such as limited local capacity, which the study confirms through TKDD's stronger effect on expenditure ($\beta = 0.977$) than PAD ($\beta = 0.729$). The high adjusted R^2 values (0.9977 and 0.9979) indicate robust models, but the Durbin-Watson statistic (1.03) suggests potential autocorrelation, possibly linked to economic shocks during the 2020-2021 pandemic, which warrants cautious interpretation.

Integrating *Maqasid Syariah* into the analysis provides a fresh perspective, emphasizing the ethical imperative of equitable resource allocation. The mediation effect supports Fahlevi et al.'s (2024) call for fiscal policies that prioritize justice and welfare, yet TKDD's insignificant direct effect raises concerns about transfer design. Wati et al. (2022) highlight Indonesia's "flypaper effect," where reliance on transfers stifles local revenue efforts, a pattern the findings confirm as TKDD's impact hinges on expenditure autonomy. Bureaucratic inefficiencies or rigid transfer conditions, as noted by Firdawaty et al. (2024), may weaken growth potential, particularly in less-developed provinces. Akita et al. (2021) further suggest that regional disparities in fiscal capacity exacerbate these challenges, underscoring the need for tailored policies. Limitations, such as inconsistent data quality across provinces and the pandemic's impact on 2020-2024 data, suggest that the results may not fully capture long-term trends. Future studies could explore sector-specific spending or extend the timeframe to better understand these dynamics.

These findings carry significant implications for policymakers aiming to align fiscal decentralization with Indonesia's 5% growth target. To embody *Maqasid Syariah* principles, policymakers should reform transfer mechanisms to prioritize performance-based allocations, encouraging investments in productive sectors like education, health, and infrastructure (Nugroho, 2022). Capacity-building programs can enhance local governments' ability to manage budgets effectively, reducing dependence on TKDD and boosting PAD generation. Strengthening accountability mechanisms, as Čajková et al. (2021) advocate, ensures transfers are spent strategically, maximizing *maslaha* and fostering equitable growth. These reforms could include incentives for provinces to develop local revenue sources and training to improve expenditure planning, addressing

regional disparities, and promoting sustainable development across Indonesia's diverse landscape.

CONCLUSION

This study reveals that fiscal decentralization significantly shapes Indonesia's regional economic growth, with expenditure autonomy playing a central role in translating revenue into tangible outcomes. PAD drives growth directly by funding productive investments, while TKDD only boosts the economy when channeled through strategic spending. The mediation effect of expenditure autonomy underscores the importance of how funds are allocated, not just their source, in fostering development across Indonesia's diverse provinces. By aligning fiscal strategies with ethical principles like wealth preservation and public welfare, this research highlights the potential for decentralization to deliver equitable growth, particularly in a Muslim-majority nation like Indonesia.

The findings carry clear implications for policymakers aiming to achieve sustainable economic progress. Reforming transfer mechanisms to prioritize performance-based allocations can ensure funds support high-impact sectors like education and infrastructure, while capacity-building programs can empower local governments to manage budgets effectively and reduce reliance on central transfers. However, limitations such as inconsistent data quality across provinces and the economic disruptions from the 2020-2021 pandemic may affect the generalizability of the results. Future research could explore how specific spending categories, like health or green infrastructure, influence growth, or extend the timeframe beyond 2024 to capture long-term trends, offering deeper insights into optimizing fiscal decentralization for Indonesia's diverse regions.

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