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THE ROLE OF GOVERNMENT FISCAL POLICY IN ENHANCING ECONOMIC GROWTH AND STATE REVENUE THROUGH THE TAXATION SYSTEM

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Abstract

Fiscal policy is one of the main instruments used by the government to manage the national economy through the regulation of state expenditure and revenue, particularly from the taxation sector. This study aims to analyse the role of government fiscal policy in promoting economic growth and increasing state revenue, with a focus on the taxation system as the main instrument. The method used is a literature review of various scientific sources, official government reports, and international institution publications. The results of the study indicate that effective fiscal policy, through productive expenditure allocation and fair and efficient taxation policies, can stimulate economic activity, increase investment, strengthen purchasing power, and expand the tax base. The tax system plays a dual role, namely as a source of development funding and as a tool for regulating economic behaviour, which, if implemented appropriately, will create a multiplier effect on economic growth. However, challenges such as low tax compliance, tax avoidance and evasion practices, and limited administrative capacity need to be addressed immediately through structural reforms, system digitalisation, and strengthening the principles of fiscal justice. Therefore, synergy between sound fiscal policies and a modern and equitable tax system is key to achieving inclusive, sustainable economic growth that supports improved public welfare.

Keywords: Fiscal policy, tax system, economic growth, government revenue, multiplier effect, fiscal justice.

Introduction

Fiscal policy is one of the main instruments used by the government in managing a country's economy. Through this policy, the government can regulate state revenue and expenditure to achieve various objectives, including maintaining economic stability, promoting growth, and ensuring a more equitable distribution of income (Harefa, 2025) . In the context of an increasingly complex global economy, fiscal policy is no longer seen merely as a tool for financing government spending, but also as a mechanism that influences the competitiveness of the national economy amid international trade flows and changes in global market dynamics (Bappenas, 2021) .

One of the most important components of fiscal policy is the tax system. Taxes are the primary source of government revenue used to finance infrastructure development, education, health, security, and various other public services (Nugroho, 2022) . In theory and practice, taxes not only contribute to government revenue but also function as an instrument for controlling economic activities through their influence on consumption, investment, and resource distribution. Therefore, the effectiveness of the tax system will greatly determine the success of fiscal policy in achieving sustainable economic growth (Wahyudi, 2023) .

Strong economic growth is a prerequisite for improving public welfare and reducing poverty. However, such growth cannot be allowed to occur naturally without appropriate policy intervention. The government, through fiscal instruments, particularly taxation, can encourage productive activities, provide incentives for the business world, and create a conducive investment climate. Conversely, ineffective tax management can cause market distortions, hinder economic activity, and even trigger fiscal instability (Chatra, 2025) .

In Indonesia, fiscal policy and the tax system play an increasingly significant role, especially in facing the challenges of the post-COVID-19 pandemic economy, commodity price fluctuations, and global geopolitical dynamics that affect trade and investment flows. Optimising tax revenue is a priority, given the increasing need for development financing amid limited resources. In this context, measured fiscal policies and an effective tax system are the backbone for maintaining macroeconomic stability while promoting growth (Jaiyesimi, 2024) .

Although the contribution of taxes to state revenue has continued to increase year on year, the challenges faced by the government are not straightforward. Issues such as low taxpayer compliance rates, tax avoidance practices, and tax evasion, as well as limitations in tax administration capacity, remain. On the other hand, there is an urgent need to create a tax system that is not only effective in terms of revenue but also fair and capable of boosting productivity in the real sector (ASEAN Policy Journal, 2023).

The relationship between fiscal policy, the tax system, economic growth, and government revenue is interdependent. For example, expansionary fiscal policy can increase government spending in strategic sectors, which in turn stimulates economic activity and expands the tax base. This expansion of the tax base increases government revenue, enabling the government to finance further development programmes. This positive cycle can be achieved if the tax system is managed according to the principles of efficiency, fairness, and legal certainty (Ulil Albab Institute, 2024) .

In the academic realm, studies on the role of fiscal policy through the tax system continue to evolve. Many previous studies have discussed the contribution of taxation to state revenue, but not all have emphasised the aspect of economic growth proportionally (Ulil Albab Institute, 2024) . This study aims to address this gap by comprehensively examining how taxation plays a dual role, as a source of government revenue and as a fiscal policy instrument that can accelerate national economic growth.

Research Method

This study employs a literature review method, which involves collecting, examining, and analysing various relevant sources of literature related to fiscal policy, the tax system, economic growth, and state revenue. Data was obtained from scientific books, research journals, official government reports, international institution publications (such as the IMF, World Bank, and OECD), as well as national statistical data released by the Central Statistics Agency (BPS) and the Directorate General of Taxes (Eliyah & Aslan, 2025) . The analysis was conducted using a descriptive-qualitative approach by comparing theories, policies, and empirical findings from previous studies, thereby providing a comprehensive overview of the role of government fiscal policy through tax instruments in promoting economic growth and increasing government revenue (Green et al., 2006) .

Results and Discussion

The Role of Fiscal Policy in Enhancing Economic Growth

Fiscal policy is one of the main instruments available to the government to influence the overall economy. Through adjustments to government spending and taxation policies, the government can regulate aggregate demand, stabilise economic cycles, and promote sustainable growth (Asroni, 2023) . Good fiscal policy management can boost economic activity during a slowdown, while controlling the symptoms of economic overheating when growth is too fast. Thus, fiscal policy plays an important role in determining the direction and speed of a country's economic development, both in the short term as a stabilisation instrument and in the long term as an engine of development (Pamungkas & Sesanti, 2023) .

The government's ability to increase state spending in strategic sectors such as infrastructure, education, health, and technology will have a direct impact on increasing productivity and production capacity of the economy. Public investment in these areas is an important foundation for long-term growth, as it can strengthen human resource quality, spur innovation, and create a more conducive business climate. In developing countries, including Indonesia, public sector spending is often the main determinant of development success because it serves to close gaps that cannot be reached by the private sector, especially in providing basic facilities and services that support economic activities (Fareed, 2023) .

Fiscal policy significantly influences economic growth through its impact on aggregate demand. Expansionary fiscal measures, such as increasing government spending or providing tax incentives, will boost disposable income and encourage consumption. This increase in consumption will prompt businesses to expand investment and production of goods and services, ultimately accelerating economic growth. The multiplier effect of fiscal spending and incentives is particularly pronounced during recessions, when the government plays a key role as the primary catalyst for economic recovery (Sulastri, 2025) .

Conversely, contractionary fiscal policies, such as reducing government spending or increasing tax rates, are implemented to dampen economic fluctuations that could trigger excessive inflation. By limiting aggregate demand growth, this measure aims to stabilise the economy and prevent the formation of asset bubbles that could jeopardise financial stability. However, the implementation of contractionary fiscal policy must be balanced and measured, as overly restrictive measures can hamper economic growth and reduce public purchasing power (Handini, 2025) .

The effectiveness of fiscal policy is largely determined by the composition of its allocation and the timeliness of its implementation. Government spending directed toward productive investments, such as infrastructure development and technological advancement, will yield greater growth impacts compared to purely consumption-oriented spending. Additionally, timely fiscal interventions are more effective in responding to economic cycle changes. Conversely, delays or misdirected planning can reduce the effectiveness of fiscal policy or even worsen an already weak economy (Budiarto, 2024) .

Tax components in fiscal policy play a dual role, namely as a source of state revenue and as an instrument to influence economic behaviour. An appropriate tax system design can encourage investment, increase labour productivity, and stimulate innovation through the provision of relevant fiscal incentives. Conversely, a complex or overly burdensome tax system can distort markets, hinder business development, and reduce investor interest (Prabowo, 2024) . Therefore, tax policy formulation must consider the balance between the state's revenue needs and the impetus for economic growth.

The impact of fiscal policy on economic growth is often measured using the concept of the fiscal multiplier, which is a measure of the change in economic output resulting from a specific change in government spending or taxes. The magnitude of the fiscal multiplier is influenced by a country's economic conditions, production capacity, as well as the type and scale of fiscal policies implemented. In a recession, the fiscal multiplier tends to be higher, so government spending will have a greater effect on growth than in normal conditions.

The sustainability aspect (fiscal sustainability) is an important consideration in the implementation of fiscal policy. Persistent budget deficits and uncontrolled increases in public debt can put pressure on long-term economic stability. Such conditions risk shifting resources from productive sectors to debt servicing, thereby reducing fiscal space for growth-promoting investments (Riawati, 2022) . Therefore, responsible fiscal management is an absolute requirement for maintaining a balance between development financing and fiscal health.

Several studies indicate that the positive impact of fiscal policy on economic growth is more pronounced in developing countries, where public investment often plays a role in complementing inadequate private sector capacity. In contrast, in developed countries, fiscal policy tends to focus more on stabilising the economic cycle rather than serving as the primary driver of growth. These differences are primarily due to the level of infrastructure maturity, production capacity, and financial sector depth of each country (Suryaman, 2025) .

Fiscal policies prioritising investment in human capital development, innovation, and infrastructure construction offer the best prospects for long-term economic growth. Such policy directions create a multiplier effect that not only increases current economic output but also strengthens the foundations for future growth. Thus, allocating a larger budget for education, research, technology, and strategic resources can transform a country's growth trajectory into a more sustainable one (Wahjoe, 2025) . However, efforts to optimise the role of fiscal policy also face various challenges, including governance issues, public spending inefficiencies, and structural rigidities in the economy. If left unaddressed, these factors will reduce the effectiveness of fiscal policy and limit its capacity to drive growth. Therefore, strengthening institutions, transparency, and accountability are integral steps in fiscal policy reform to achieve optimal development goals (Manggala, 2024) .

Finally, to achieve optimal economic results, fiscal policy must be implemented synergistically with monetary policy and other structural reform programmes. A comprehensive approach—combining short-term stabilisation with long-term development priorities—will create a healthy, productive, and adaptive economic ecosystem that can withstand global challenges. Synergy between these policies will result in more stable economic growth while improving the welfare of the people evenly.

The Tax System as an Instrument for Increasing State Revenue

The tax system is one of the most crucial fiscal instruments in promoting increased state revenue. Taxes, as the primary source of government revenue, have a fundamental function in financing public expenditures, including infrastructure development, the provision of basic services, and the fulfilment of other national needs. Therefore, the effectiveness of the tax system in collecting revenue is crucial to the government's fiscal capacity to fulfil its role as a provider of essential public goods and services for economic growth and the welfare of the community (Jasiyah, 2024) .

Taxation not only serves as a tool for revenue collection but also as a policy instrument that can influence economic structure and the behaviour of economic actors. With appropriate taxation policies, the government can provide incentives or disincentives for certain sectors, regulate income distribution, and maintain macroeconomic stability (OECD, 2025) . Therefore, the taxation system must be designed in such a way that it is not only effective in terms of revenue, but also fair and capable of supporting productive economic activities.

Various types of taxes have different characteristics and roles in increasing state revenue. Income tax, both from individuals and businesses, is one of the main sources of revenue that reflects the economic capacity of taxpayers. Value-added tax (VAT) and import duties also contribute significantly, especially from consumption and international trade. The selection and management of proportional and non-burdensome tax types will determine the success of the tax system as a fiscal instrument.

Optimising tax revenue faces numerous challenges, including low taxpayer compliance, tax evasion and avoidance, and limited tax administration capacity. Low public awareness and compliance with tax obligations result in untapped potential for state revenue. Therefore, enhancing the effectiveness of oversight, tax education, and administrative reform are strategic steps that are equally important (Setiawan, 2024) .

Another significant challenge is the practice of tax avoidance and tax evasion, which cause substantial losses to state finances. The government needs to strengthen regulations and taxation mechanisms that can identify and take action against non-compliant parties without imposing excessive burdens that could hinder the business climate. The use of information technology and data analytics can strengthen the administration's ability to detect and collect taxes, thereby reducing revenue leakage (Yuda, 2024) .

An effective tax system must also be built on the principle of fiscal justice, meaning that taxes must be levied proportionally to the economic capacity of taxpayers. The application of the principle of progressivity in income tax, for example, can function as a tool for income redistribution to reduce social inequality and promote economic inclusion. Thus, taxation is not only oriented towards state revenue but also supports inclusive and sustainable growth. (Yusuf, 2022) .

The structure and design of tax rates significantly influence taxpayer behaviour and macroeconomic impacts. Excessively high rates can increase incentives for tax avoidance and hinder investment, while excessively low rates reduce the potential for government revenue. Therefore, tax rate determination must be based on careful analysis, taking into account national economic conditions, purchasing power, and the competitiveness of business sectors (Jasiyah, 2024) .

A modern and efficient tax administration system is essential to support optimal tax management. Strengthening tax institutions through the digitalisation of tax reporting and payment processes, inter-agency data integration, and improving risk management systems are important efforts to enhance compliance and service to taxpayers. Additionally, transparency and accountability in tax management will strengthen public trust in the tax system (Wang, 2025) .

The importance of policy coherence between the tax system and overall fiscal policy must be a key priority. Adequate tax revenue provides fiscal space for financing development and social programmes, which in turn contributes to economic growth. Conversely, poor tax administration can lead to budget deficits and excessive reliance on other unstable sources of revenue, thereby creating fiscal risks (Mutia et al., 2025) .

Global economic developments and rapid digitalisation require tax systems to be adaptive and responsive to new conditions, such as the growing digital economy and e-commerce. Governments must formulate relevant and innovative tax policies to capture revenue from cross-border and technology-based economic activities without hindering innovation and investment (Jusuf, 2021) .

Comprehensive tax reform, including improving the tax base, expanding the tax base, and eliminating misdirected incentives, is an important step in increasing state revenue. Tax policy adjustments must be made in a sustainable manner with in-depth impact assessments to ensure that the resulting policies are effective and fair. Collaboration between the government, the private sector, and civil society is also vital in creating an effective tax system. Taxpayers' awareness and active participation in fulfilling their fiscal obligations should not only be driven by regulations but also by good education and communication about the benefits of taxes for national development (Sulistyo, 2022) .

Overall, an effective and efficient tax system is the backbone of state funding for sustainable development. By strengthening tax mechanisms and improving taxpayer compliance through fair policies and professional administration, the government will be able to increase state revenue, which will ultimately strengthen fiscal stability and promote sustainable national economic growth.

Conclusion

Government fiscal policy, particularly through taxation instruments, has proven to play a strategic role in driving economic growth while increasing state revenue. Through proper management of state expenditure and the formulation of appropriate taxation policies, the government is able to influence aggregate demand, expand production capacity, and create a conducive economic climate for investment. Expansionary fiscal policies during a recession can accelerate economic recovery, while appropriate contractionary policies during an economic boom can maintain price stability and avoid the risk of excessive inflation. The success of fiscal policies in driving economic growth depends heavily on the composition of productive spending, the timeliness of implementation, and synergy with other economic policies.

The tax system, as one of the main pillars of fiscal policy, serves a dual function—as a source of state revenue and as an instrument for regulating economic behaviour.

Taxes provide funds that are used to finance infrastructure development, education, health, and various public services that form the foundation of long-term economic growth. Additionally, through the design of proportional tax rates and the provision of targeted fiscal incentives, the government can encourage priority sectors to grow faster. However, the effectiveness of this system is not without challenges, such as low taxpayer compliance, tax avoidance and evasion practices, and limited tax administration capacity. Therefore, sustainable tax reform, strengthening digital-based administration systems, and applying fiscal justice principles are crucial steps to optimise state revenue without hindering growth.

Overall, the relationship between fiscal policy, economic growth, and government revenue is mutually reinforcing as long as these policies are well designed, effectively implemented, and transparently monitored. Increased revenue through an efficient tax system provides greater fiscal space for the government to undertake productive investments, which in turn expands the tax base and strengthens the country's finances in the future. Thus, sound fiscal policy, supported by a fair and modern tax system, is not only a short-term economic stabilisation tool but also a key driver of inclusive, sustainable economic growth that improves the well-being of society as a whole.

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