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# THE EFFECT OF CAPITAL EXPENDITURE, LOCAL REVENUE, AND EMPLOYEE EXPENDITURE ON LOCAL GOVERNMENT FINANCIAL PERFORMANCE

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**Abstract**

This research investigates the determinants of Financial Performance in District/City Gove rnments in West Java (2021-2024). Using Institutional Theory and a quantitative approach, the study analyzes 99 observations from audited Budget Realization Reports (LRA). The regression model is highly robust 96.7% is the coefficient of determination (R). The results reveal that Locally-Owned Revenue (PAD) has a positive and significant effect and serves as the primary driver of execution. Conversely, Capital Expenditure and Personnel Expenditure exert significant negative pressure, reflecting fiscal rigidities and high maintenance burdens. While PAD is a component of the autonomy ratio, its positive impact reflects genuine managerial capacity in internalizing decentralization pressures. The study recommends prioritizing PAD digitalization and conducting rigorous spending reviews to enhance fiscal efficiency.

**Keywords**: Capital Expenditure, Local Original Revenue, Employee Expenditure, Financial Performance

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## INTRODUCTION

The implementation of fiscal decentralization has made regional financial performance a primary focus, requiring local governments to enhance independence while guaranteeing accountability and openness in the administration of financial resources. This is reinforced by Law Number 1 of 2022 concerning Financial Relations between the Central Government and Regional Governments (HKPD), which updates previous regulations and introduces significant changes by expanding decentralization in budget planning and oversight, with the main objective of achieving fiscal independence through the optimization of Regional Original Revenue (PAD) and more efficient expenditure management (Republik Indonesia, 2022). Regional financial performance, however, is not merely reflected in numerical outcomes but represents the government's ability to utilize resources efficiently to achieve development goals (Ramadana et al., 2023), and from an Institutional Theory perspective, it is often influenced by pressures to gain public and institutional legitimacy, such as obtaining an Unqualified Opinion (WTP) from the Supreme Audit Agency (BPK) (Putri, Ria Dwi, 2025), although this pursuit of legitimacy may conflict with the reality of less optimal budget structures.

The fiscal condition of the West Java Provincial Government in 2024 showed notable irregularities, where the APBD Accountability Report recorded revenue exceeding the target at IDR 36.68 trillion (101.08%), largely supported by Locally-Owned Revenue (PAD) of IDR 25.31 trillion, indicating strong fiscal capacity at the provincial level; however, this strength is not evenly distributed across the 27 regencies/cities, many of which still face structural challenges such as dependence on central transfer funds and limited spending flexibility. A key issue in the fiscal structure lies in suboptimal expenditure composition, as operational spending particularly personnel expenditure dominated with IDR 19.98 trillion, creating fiscal rigidity that restricts investment in productive sectors, while capital expenditure was relatively low at IDR 2.11 trillion, potentially hindering infrastructure development and the optimization of public services in West Java.

**Table 1.**
**Summary of Realization of Revenue and Expenditure of the West Java Provincial Government in 2024**

| Total Income | Realization (%) | PAD Contribution | Employee Expenditure | Capital Expenditure |
|---|---|---|---|---|
| Rp 36,68 T | 101,08% | Rp 25,31 T | Rp 19,98 T | Rp 2,11 T |

Source: DPMPTS (Provinsi Jawa Barat, 2024)

The inconsistency of previous research findings was a strong reason for conducting this study. (Atmoko & Khairudin, 2022; Mubarok et al., 2022) found a significant positive effect of capital expenditure on local government financial performance, while (Sutisman et al., 2024) showed a significant negative effect of capital expenditure. (Ardelia et al., 2022; Natalia Padang et al., 2023) found no significant effect of capital expenditure. Meanwhile, (Atmoko & Khairudin, 2022; Natalia Padang et al., 2023) found that local revenue (PAD) positively impacted financial performance, but (Azhar & Si, 2021; Simamora & Budiwitjaksono, 2022) found the opposite. Interestingly, personnel expenditures are rarely considered a performance determinant in these studies, even though this component constitutes the largest portion of the regional budget.

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Based on the aforementioned phenomena and this research is to examine the contribution of local revenue (PAD). capital expenditure, and personnel expenses to the financial performance of local governments in West Java Province for the 2021-2024 period. The results are expected to provide theoretical contributions to strengthening institutional theory in public finance and provide practical input for local governments in designing more proportional and accountable budget policies.

Based on the context, this research focuses on analyzing factors that potentially influence Local governments' financial performance in the Province of West Java, considering the discrepancies between budget targets and realizations across regencies/cities and the suboptimal management of regional revenues and expenditures, which necessitate empirical testing of relevant financial variables. Accordingly, the study formulates the problem to examine whether Regional Original Revenue (PAD), Capital Expenditures, and Personnel Expenditures affect financial performance both partially and simultaneously during the 2021–2024 period, with the objective of providing a deeper empirical understanding of how these variables contribute to local government financial performance. Furthermore, This research is expected to offer theoretical, practical, and policy benefits by contributing to the development of Institutional Theory (Silva et al., 2024) through demonstrating how norms, bureaucratic structures, and budget policies influence financial performance, as well as expanding insights into public sector financial determinants, particularly in economically active regions like West Java; practically, it can guide provincial and district/city governments in designing more effective, efficient, and outcome-oriented financial management strategies while emphasizing the importance of balancing PAD growth, controlling personnel expenditures, and optimizing capital expenditures for sustainable fiscal performance; and from a policy perspective, it can serve as a reference for APBD preparation and regional fiscal policies, while supporting BPKAD and Bappeda in strengthening performance-based budgeting, enhancing transparency, and improving accountability to achieve better governance.

## REVIEW OF LITERATURE

This study is based Meyer and Rowan developed institutional theory (1977), which explains that the behavior of public organizations, including provincial governments, is driven not only by economic efficiency but also by the need to gain legitimacy from the institutional environment, including central regulations, governance norms, and societal demands; in the context of regional financial management in West Java, this theory provides a framework to understand how such pressures influence government behavior in managing revenue, expenditure, and financial accountability. Accordingly, capital expenditures reflect responses to institutional pressures to enhance public legitimacy through infrastructure development, locally generated revenue (PAD) indicates the ability to demonstrate fiscal independence in line with decentralization principles, and Employee Expenditure represent internal bureaucratic pressures and efficiency in governance, all of which collectively influence local governments' financial performance.

### Capital Expenditure

Capital expenditure in this study is grounded in Institutional Theory, which explains that public organizations act not only for efficiency but also to gain external legitimacy through visible development outcomes. In the context of local governments in West Java, capital expenditure reflects a response to institutional pressures to demonstrate achievements in physical development and public services (DiMaggio & Powell, 1983). Conceptually, it refers to spending that generates fixed assets with long-term economic benefits, enhances regional wealth (Al Hidayat & Bima Eka Putra, 2025) and includes expenditures with a useful life exceeding one fiscal year aimed at increasing public service capacity through capital utilization and investment growth (BPK, 2010), while also representing fiscal accountability in meeting infrastructure demands (Sefira & Budiwitjaksono, 2022; Simamora & Budiwitjaksono, 2022; Taufik Hidayat, Maulina Dyah Permatasari, 2024). Within this framework, increasing capital expenditure reflects efforts to fulfill normative and mimetic pressures to appear legitimate, professional, and service-oriented (Silva et al., 2024), thereby enhancing public trust and legitimacy, improving service quality, and attracting investment, which is expected to positively influence financial performance; this view is supported by empirical findings (Atmoko & Khairudin, n.d.; Mubarok et al., 2022) showing that productive capital expenditure significantly improves financial performance by stimulating regional economic activity, leading to the formulation of the hypothesis that capital expenditure has a positive effect on local government financial performance (H1).

**Local Revenue**

Local Revenue (PAD) in this study is grounded in Institutional Theory, which posits that public organizations seek legitimacy through compliance with institutional rules and norms (Putri, Ria Dwi, 2025) within this framework, PAD reflects regional fiscal independence as an implementation of financial decentralization, as defined in Law No. 33 of 2004, where it represents revenue derived from local economic potential through regional regulations. PAD also indicates the ability of local governments to optimally manage regional resources (Atmoko & Khairudin, 2022) and serves as a primary determinant of fiscal independence (Nopia Yudiastuti et al., 2025). From an Institutional Theory perspective, increasing PAD is a response to coercive pressure from the central government to reduce reliance on transfer funds and maximize local potential as a form of fiscal responsibility (Noeng et al., 2023), leading regions with higher PAD, such as those in West Java, to be perceived as more legitimate due to their capacity to implement fiscal autonomy, enhance accountability, and manage resources transparently; consequently, PAD is a strategic variable influencing financial performance. This perspective underlies the development of the second hypothesis, where local governments strive to increase PAD to comply with decentralization norms and strengthen legitimacy, with higher PAD reflecting stronger financial capacity and independence, as supported by empirical findings (Mubarok et al., 2022; Natalia Padang et al., 2023; Noviana Sri Hastuti, 2024) showing a significant positive effect of PAD on financial performance, leading to the hypothesis that Regional Original Revenue (PAD) positively affects local government financial performance (H2).

**Employee Expenditure**

In this study, Employee Expenditure are explained through Institutional Theory as a response to internal institutional pressures within the local government bureaucracy, where such expenditures represent compensation and rewards for state officials as key actors in public service delivery; based on Law Number 45 of 2007, they include salaries, allowances, and other forms of compensation, and function as instruments to enhance performance,

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productivity, and service quality (Sefira & Budiwitjaksono, 2022; Simamora & Budiwitjaksono, 2022). From this perspective, the allocation of Employee Expenditure reflects normative and structural pressures that require local governments in West Java to balance efficiency and employee welfare to maintain bureaucratic stability (Putri, Ria Dwi, 2025), while also supporting operational effectiveness (Nabila et al., 2025; Rofiq & Arza, 2021) and being measured through indicators such as base salary, allowances and incentives, pension costs, social security, and training costs (Hatmi et al., 2022), so that efficient management reflects the government's ability to respond to institutional demands while maintaining credibility. Theoretically, adequate employee expenditure is expected to increase motivation and productivity, support effective financial management, prevent inefficient behavior such as corruption, and promote professional governance, thereby contributing to sound financial performance; thus, despite mixed empirical findings, this study assumes that employee welfare is positively related to productivity and organizational health, leading to the formulation of the third hypothesis that Employee Expenditure has a positive impact on regional government financial performance (H3).

**Financial Performance of Regional Government**

Regional government financial performance serves as the dependent variable in this study and is explained using Institutional Theory, which emphasizes how institutional pressures shape fiscal behavior; financially, performance reflects the achievement of government policies and programs measured through budget utilization (Khadijah Dinda Putri Dewi, 2022), functions as a key benchmark for evaluating effectiveness and accountability in financial management (Simamora & Budiwitjaksono, 2022), and indicates the ability of local governments to optimize regional economic potential for long-term fiscal sustainability (Atmoko & Khairudin, 2022). Within this framework, strong financial performance represents not only technical efficiency but also the ability of regional governments to meet normative and regulatory expectations, as institutional pressures encourage governments in West Java Province to present transparent and accountable financial outcomes in line with good governance principles to gain legitimacy from the public and supervisory institutions (Saripudin, 2025); thus, this theory provides a conceptual basis for understanding how capital expenditure, PAD, and employee expenditure influence financial performance as part of fulfilling institutional standards.

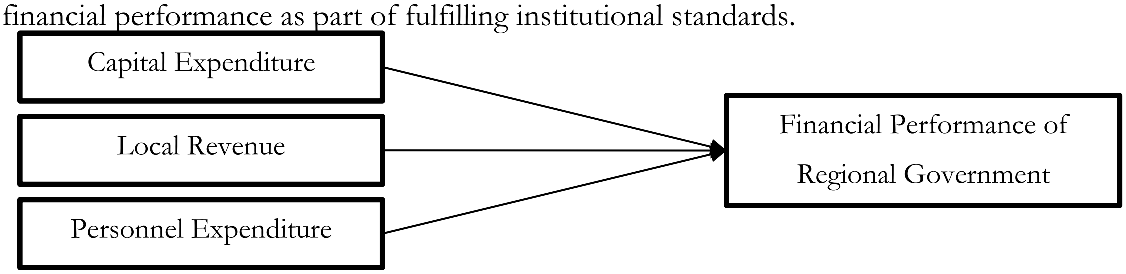


**Figure 1.**
**Conceptual Framework**

## RESEARCH METHOD

This research employs a quantitative approach utilising secondary numerical Data collected from regency Budget Realisation Reports (LRA) city governance in West Java

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Province during the period from 2021 to 2024 published by the Supreme Audit Agency (BPK). The study initially consisted of 108 observations representing 27 regencies/cities in West Java Province over the period 2021–2024. During the normality testing stage, nine observations were identified as extreme outliers using the standardized residual method with a threshold of ±2.5 and were subsequently excluded to satisfy the normality assumption. Consequently, the final sample used in the regression analysis consisted of 99 observations. The regional financial independence ratio assesses financial performance. This analysis employs pooled multiple regression analysis using SPSS to inspect the effect of Capital Expenditure, Local Revenue (PAD), and Employee Expenditure on regional financial performance. The analysis includes descriptive statistics, Classical assumption tests and hypothesis tests.

**Population and Sample**

The population in this research consists of the Regional Government Financial Reports (LKPD) of regencies and municipalities in West Java Province, as presented in the Budget Realization Report (LRA) of the APBD for the 2021–2024 period, selected due to the diversity of regional economic characteristics and fiscal capacities, which is expected to provide a comprehensive view regarding the impact of Capital Expenditure, Local Revenue (PAD), and Personnel Expenditures about Financial Performance. The sample was determined using purposive sampling to ensure relevance and data completeness, with criteria including regency and city governments that consistently published LRA reports from 2021 to 2024, reports that the Supreme Audit Agency (BPK) has conducted an audit and officially published, and financial statements containing complete data for every research factor, including capital expenditure, PAD, Employee Expenditure, and Financial Performance indicators, thereby ensuring the suitability of the sample for empirical analysis of variable relationships.

**Data Sources and Data Collection**

This analysis utilizes secondary numerical data obtained from official documents, enabling systematic analysis to examine relationships between variables, support objective measurement, and facilitate processing using SPSS; the data include budget realization figures for Capital Expenditures, Regional Original Revenue (PAD), and Employee Expenditure from the Budget Realization Report (LRA), financial performance data derived from financial reports to calculate ratios such as independence and effectiveness, and regional data covering all regencies and cities in West Java Province as the unit of analysis, with sources drawn from audited Regional Government Financial Reports Learning Implementation Plan (LKPD) for the period of 2021 to 2024 by the Supreme Audit Agency (BPK) and from the Directorate General of Fiscal Balance (DJPK) through sipd.kemendagri.go.id or djpk.kemenkeu.go.id, all of which are official, published, audited, and compliant with government accounting standards, making them suitable for quantitative research. Data collection is conducted documentation methods, as the data are publicly available in LKPD, and involves identifying all regencies and cities that consistently publish APBD realization reports during 2021–2024, accessing and downloading audited reports via DJPK or regional portals, extracting relevant figures for Capital Expenditure, PAD, and Employee Expenditure while calculating financial performance ratios, organizing the data into a panel dataset (27 regions cross-section and 4-

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year time series) for SPSS analysis, and verifying completeness and consistency to ascertain the correctness of statistical outcomes.

**Table 2.**
**Operational Variables**

| Variable | Measurement Indicators | Scale |
|---|---|---|
| Capital Expenditure (Saripudin, 2025) | Total Capital Expenditures in the Budget Implementation Report (BIR) | Ratio |
| Local Revenue (LOSR) (Rosnidah, 2018; Saripudin, 2025) | Total Local Own-Source Revenue Realization (Local Taxes, Fees, Local Asset Proceeds, etc.) | Ratio |
| Personnel Expenditures (PE) (Collins et al., 2021) | Total Actual Personnel Expenditures (Salaries, Allowances, Honoraria) | Ratio |
| Financial Performance of Regional Government (Farhani & Rosnidah, 2018) | $Financial\ Performance = \frac{Local\ Revenue}{Transfer\ Revenue} \times 100\%$ | Ratio |

## RESULTS AND DISCUSSION

This study focuses on the West Java Provincial Government, utilizing supplementary data in the format of the Regional Budget Implementation Reports for the 2021–2024 period, with a sample size of N=108. After applying a natural logarithm (LN) transformation and data cleaning to address non-normally distributed data, the valid sample size for analysis comprised 99 observations (N=99) (Sugiyono, 2024).

Results of Descriptive Statistical Analysis

Descriptive statistical examination was used to provide an overview of each research variable's minimum, maximum, mean, and standard deviation. that had been transformed into Natural Logarithm (LN) form.

**Table 3.**
**Descriptive Statistics Before Outliers**

| | N | Min | Max | Mean | Std.Deviation |
|---|---|---|---|---|---|
| Capital Expenditure | 108 | 24,49 | 28,20 | 26,6505 | 0,78605 |
| Local Revenue | 108 | 25,57 | 29,01 | 27,2829 | 0,82909 |
| Personnel Expenditure | 108 | 26,59 | 31,07 | 27,8414 | 0,58851 |
| Financial Performance of Regional Government | 108 | 15,89 | 20,78 | 19,4485 | 0,82245 |
| Valid N (listwise) | 108 | | | | |

According to the results of the descriptive the analysis, that can be seen that the lowest capital expenditure value of 24.49 was recorded in Ciamis Regency in 2024. The highest capital expenditure value of 28.20 was recorded in Bogor Regency in the period 2021. The mean capital expenditure from 2021 to 2024 is 26.6505. The low level of capital expenditure reflects the average limitations Local governments in West Java Province in allocating funds for physical infrastructure development. With adequate facilities and infrastructure, local governments can be more effective in boosting economic growth for their communities.

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The second variable is Local Revenue (PAD), with the lowest value recorded in Tasikmalaya Regency in 2023 at 25.57. The highest PAD value was recorded in Bekasi City in 2024 at 29.01. The average PAD value from 2021 to 2024 was 27.2829. The still-low PAD value is due to suboptimal revenue from the local tax and retribution sectors, so the West Java Provincial government remains heavily dependent about the flow of funding from the central government.

The lowest value for personnel expenditure was 26.59, recorded in the City of Banjar in 2021. Meanwhile, the highest value for personnel expenditure was 31.07, recorded in Bogor Regency in 2022. The average personnel expenditure for the period from 2021 to 2024 is 27.8414. Local government spending in West Java Province, which is still dominated by personnel expenditure, limits the budgetary flexibility for the infrastructure sector. If efficiency measures are implemented in this routine expenditure category, local governments will have greater fiscal space to improve financial performance and accelerate more productive regional development.

Based on the analysis results, the lowest value of 15.89 was recorded in Tasikmalaya Regency in 2023. Meanwhile, the highest value of 20.78 for Financial Performance was recorded in Bekasi City in 2024. The average Financial Performance score for the 27 Regencies/Cities in West Java Province in the 2021–2024 period was 19.4485. This relatively high average, which is close to the maximum value, indicates efforts to optimize the financial performance of local governments in West Java during the observation period. The huge disparity between the minimum and greatest values reflects disparities among regions, with cities being more stable than regencies in West Java.

**Results of the Classical Assumptions Test**

The normality test seeks to ascertain if the residuals in the regression model have a normal distribution. The outcomes of the normalcy assessment are shown in the subsequent table:

**Table 4.**
**Normality Test Before Outliers**

| | | |
|---|---|---|
| N | | 108 |
| Normal Parameters[a,b] | Mean | ,0000000 |
| | Std. Deviation | ,63668486 |
| Most Extreme Differences | Absolute | ,317 |
| | Positive | ,199 |
| | Negative | -,317 |
| Test Statistic | | ,317 |
| Asymp. Sig. (2-tailed)[c] | | <,001 |

**Table 5.**
**Normality Test After Outliers**

| | | |
|---|---|---|
| N | | 99 |
| Normal Parameters[a,b] | Mean | ,0000000 |
| | Std. Deviation | ,114665568 |
| Most Extreme Differences | Absolute | ,089 |

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| | | |
|---|---|---|
| | Positive | ,048 |
| | Negative | -,089 |
| Test Statistic | | ,089 |
| Asymp. Sig. (2-tailed)[c] | | ,052 |

The Kolmogorov-Smirnov test table shows a significant improvement after outliers were removed. Before cleaning, the data with a sample size of 108 had an Asymp. Sig. (2-tailed) <.001, which means the data were not normally distributed because the significance value was well below 0.05. However, after outliers were removed, reducing the sample size to 99, the Asymp. Sig. (2-tailed) value increased to 0.052. Since this significance value is now greater than 0.05 (0.052 > 0.05), it can be concluded that the residual values in this research model satisfy the assumption of a normal distribution.

**Multicollinearity Test**

A multicollinearity test is executed to ascertain whether there are relationships between the independent variables in the model. An effective regression model should be free of multicollinearity. The test results are shown in the subsequent table:

**Table 6.**
**Multicollinearity Test**

| Model | | Coefficients | Collinearity Statistics |
|---|---|---|---|
| | | Tolerance | VIF |
| 1 | (Constant) | | |
| | Capital Expenditure | ,322 | 3,101 |
| | Local Revenue | ,329 | 3,040 |
| | Personnel Expenditure | ,320 | 3,128 |

The outcomes of the multicollinearity assessment, as shown indicate that there is no significant correlation among the independent variables in the table.
This is evidenced by the Tolerance values for the Expenditures (0.322), Regional Revenue (0.329), and Personnel Expenditures (0.320) variables, all of which are greater than 0.10. Meanwhile, the values of the Variance Inflation Factor (VIF) each variable are 3.101, 3.040, and 3.128, all of which are less than 10 (< 10). Thus, It can be concluded that multicollinearity is an absent issue among the independent variables in our regression model; the model is free from multicollinearity.

**Table 7.**
**Spearman's rho heteroscedasticity test**

| Correlations | | | | | | |
|---|---|---|---|---|---|---|
| | | | Capital Expenditure | Local Revenue | Personnel Expenditure | Unstandardized Residual |
| Spearman's rho | Capital Expenditure | Correlation Coefficient | 1,000 | ,720 | ,700 | ,017 |
| | | Sig.(2-tailed) | , | <,001 | <,001 | ,868 |
| | | N | 99 | 99 | 99 | 99 |
| | Local Revenue | Correlation Coefficient | ,720 | 1,000 | ,718 | -,112 |

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| | | | | | | |
|---|---|---|---|---|---|---|
| | | Sig.(2-tailed) | <,001 | , | <,001 | ,269 |
| | | N | 99 | 99 | 99 | 99 |
| | Personnel Expenditure | Correlation Coefficient | ,700 | ,718 | 1,000 | -,086 |
| | | Sig. (2-tailed) | <,001 | <,001 | , | ,395 |
| | | N | 99 | 99 | 99 | 99 |
| | Unstandardized Residual | Correlation Coefficient | ,017 | -,112 | -,086 | 1,000 |
| | | Sig. (2-tailed) | ,868 | ,269 | ,395 | , |
| | | N | 99 | 99 | 99 | 99 |

According to the table above, which presents the outcomes of the heteroscedasticity test using Spearman's rho correlation, it can be seen that the regression model confirms the assumption of non-heteroscedasticity. This is evidenced by the significance values (2-tailed sig.) of each independent variable relative to the unstandardized residuals, which are all above the significance threshold of 0.05. Specifically, the Capital Expenditure variable yields a significance value of 0.868, the Local Revenue variable shows a value of significance 0.269, and the Capital Expenditure variable has the highest value of significance at 0.395.

With a sample size of 99 observations, these significance values, which far exceed the 0.05 threshold, indicate that there is no significant association or correlation found between the independent variables and their residual values. Therefore, it can be concluded which regression the model is devoid of heteroscedasticity, so the resulting estimator is a Best Linear Unbiased Estimator (BLUE), and the outcomes of the subsequent hypothesis tests can be considered valid and unbiased.

**Autocorrelation Test**

**Table 8.**
**Autocorrelation Test**

| Model Summary[b] | | | | | |
|---|---|---|---|---|---|
| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate | Durbin-Watson |
| 1 | ,984[a] | ,967 | ,966 | ,11646 | 1,199 |

Based on the table above, the Durbin–Watson statistic obtained is 1.199. Although this value falls within the acceptable range of 0 to 4, it should be interpreted with caution. In the Durbin–Watson test, a value close to 2 generally indicates that there is no autocorrelation problem in the regression model. Thus, a value of 1.199 indicates that the regression model does not show strong evidence of serious autocorrelation. However, the possibility of mild positive autocorrelation cannot be completely ruled out, so this result still needs to be considered in the overall evaluation of the model (Ghozali, 2021; Gujarati & Porter, 2009).

**Partial Test (t-Test)**

**Table 9.**
**Partial Test (t-Test)**

| | | B | t | Sig. |
|---|---|---|---|---|
| Model 1 | (Constant) | | | |

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| | | | |
|---|---|---|---|
| Capital Expenditure | -,257 | -9,309 | ,000 |
| Local Revenue | 1,291 | 50,340 | ,000 |
| Personnel Expenditure | -1,056 | -25,316 | ,000 |

The effect of Capital Expenditures on Financial Performance has a regression coefficient (B) of -0.257 with a negative direction and a significance level of 0.001. It can be concluded that Capital Expenditures have a negative and significant effect.

The effect of Local Own-Source Revenue on Financial Performance has a regression coefficient (B) of 1.291 with a positive direction and a significance level of (0.001). It can be stated that Local Revenue exerts a positive and considerable impact.

The effect of Personnel Expenditures on Financial Performance has a t-value of -1.056 with a negative direction and a significance level of (0.001). It can be concluded that profitability has a negative and substantial impact.

**Coefficient of Determination ($R^2$)**

The Coefficient of Determination test is performed to The extent of the independent variable explains the variation in the dependent variable. Based on the outcomes of the coefficient of determination assessment, the R-squared value is 0.967. This signifies that 96.7% of the fluctuation in the dependent variable (financial performance) is explained by the combination of the independent variables (Capital Expenditures, Local Revenue, and Personnel Expenditures). Meanwhile, the remaining 3.3% is by additional variables external to this research model. The high coefficient of determination denotes that the independent variables collectively explain a substantial proportion of the variation in regional financial performance.

**Discussion**

This document presents a comprehensive analysis of the impact of Capital Expenditures, Local Revenue, and Personnel Expenditure on the Financial Performance of the West Java Regional Government from 2021 to 2024, based on hypothesis testing through multiple linear regression analysis.

**The Effect of Capital Expenditures on Financial Performance**

The statistical analysis indicates that the Capital Expenditure variable possesses a negative regression coefficient of -0.257, with a significance level of 0.001. Given that the significance value is below 0.05, Capital Expenditure exerts a substantial influence on financial performance. Consequently, due to the negative regression coefficient, the first hypothesis (H1), which anticipated a positive effect, is dismissed. These data imply that any increment in capital expenditure allocation tends to reduce local government financial performance in the current year.

Within the framework of Institutional Theory, this phenomenon can be explained as a response to mimetic isomorphism pressures, where local governments compete to build physical assets and infrastructure to secure symbols of development legitimacy, even if such investments are not necessarily fiscally efficient. Large fixed assets require high maintenance and depreciation costs, which, if not offset by a rapid return on assets, will burden the budget structure and reduce the efficiency of short-term financial ratios.

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In addition, the benefits generated from capital expenditure generally emerge over a longer period, whereas financial performance indicators often capture short-term fiscal outcomes. Infrastructure projects that are not yet fully utilized or are still in the development phase may create immediate fiscal burdens before generating measurable economic returns. Consequently, inefficient project implementation and underutilized assets may contribute to lower short-term financial performance ((Sutisman et al., 2024).

The findings of this study align with those of (Budiharjo et al., 2025; Noviana Sri Hastuti, 2024a; Sutisman et al., 2024), who also that capital spending is detrimental impact on financial performance. This consistency in results indicates that large-scale capital expenditure without productive asset management can become a fiscal burden. These results contradict the findings of (Atmoko & Khairudin, 2022; Mubarok et al., 2022; Ramadana et al., 2023), who concluded that there is a significant positive effect. This discrepancy is likely due to the characteristics of budget absorption efficiency in West Java, where the share of capital expenditure is relatively small (an average of Rp2.11 trillion) compared to operational expenditure, so that its economic leverage has not been able to instantly offset its expenditure burden in the financial statements.

**The Effect of Local Revenue on Financial Performance**

The statistical analysis indicated that the Local Revenue (PAD) variable exhibited a regression coefficient (b) of 1.291 with a significance level of 0.001, so validating the second hypothesis (H2) statistically. Although PAD is mathematically a numerator component in the autonomy ratio, this finding is not tautological but rather reflects actual managerial capacity.

Within the framework of Institutional Theory, the calculated t-value (50.340) indicates the local government’s success in internalizing the coercive pressures of decentralization into credible fiscal autonomy. Although PAD constitutes an important component of the regional financial independence ratio, the positive relationship observed in this study should be interpreted cautiously due to the potential for mechanical association between the independent and dependent variables. Nevertheless, PAD remains an important indicator of local governments’ ability to respond to coercive pressures arising from fiscal decentralization policies and to strengthen fiscal autonomy through local revenue optimization (Rosnidah, 2018; Silva et al., 2024). These findings indicate that PAD, capital expenditure, and personnel expenditure jointly play important roles in explaining variations in local government financial performance in West Java.

These research results align with (Ginting et al., 2024; Neneng Widowati et al., 2024; Simamora & Budiwitjaksono, 2022), which indicate that Local Own-Source Revenue (PAD) has a significant positive effect on local government financial performance, as measured by autonomy, fiscal decentralization, or the routine capacity ratio. However, these results contradict the findings of (Aslindar & Hapsari, 2022; Azhar & Si, 2021), which state that Local Own-Source Revenue has no effect, thereby demonstrating that in West Java, PAD plays a crucial role as the primary driver of fiscal capacity.

**The Effect of Employee Expenses on Financial Performance**

According to the findings of statistical testing, the Employee Expenditure variable showed a negative regression coefficient with a significance value of 0.001. As the significance value is below 0.05, Employee Expenditure have a significant negative effect on financial

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performance. Therefore, the third hypothesis (H3), which predicted a positive effect of Employee Expenditure on financial performance, is rejected.

This finding is consistent with institutional theory, where Employee Expenditure serve as a response to normative pressures aimed at ensuring the well-being of the bureaucracy. However, without efficient governance, the size of this expenditure can become a burden that weakens financial health, regardless of its role in maintaining internal stability. This explains the phenomenon that the dominance of employee expenditure, which exceeds Rp19.98 trillion, clearly constricts the regional budget. This limits the government's flexibility to redirect funds to more productive sectors.

Selain itu, belanja pegawai yang terlalu tinggi dapat menimbulkan rigiditas fiskal karena mengurangi fleksibilitas pemerintah daerah dalam mengalokasikan anggaran untuk investasi produktif dan program pembangunan. Dominasi belanja rutin pegawai dalam anggaran berpotensi membatasi pembangunan infrastruktur serta inovasi layanan publik, terutama jika peningkatan belanja tersebut tidak diikuti oleh perbaikan kinerja pemerintah secara proporsional (Rofiq & Arza, 2021).

This finding offers a new perspective that differs from the assumption (Sefira & Budiwitjaksono, 2022) that personnel expenditures drive productivity, as data from West Java actually indicates the inefficiency of bureaucratic costs within the APBD structure.

## CONCLUSION

According to the findings of the data analysis and discussion regarding the determinants of local government financial performance in West Java Province for the 2021–2024 period, it can be concluded that the structure of local financial management has a very strong impact on financial performance outcomes. Collectively, the variables of Capital Expenditures, Local Own-Source Revenue (PAD), and Personnel Expenditures account for 96.7% of the variation in local government financial performance. This demonstrates that the combination of revenue autonomy and expenditure allocation policies constitutes the primary pillar in determining the fiscal health of local governments, consistent with the framework of Institutional Theory.

Specifically, this study concludes that Local Own-Source Revenue (PAD) is the only variable that contributes positively to improved financial performance. The greater the ability of regencies and cities in West Java to tap into local economic potential, the higher their degree of financial autonomy and performance. Conversely, Capital Expenditures were found to have a negative effect, suggesting that the physical asset investments currently undertaken by local governments still burden the short-term budget structure due to high maintenance costs and depreciation, and have not yet yielded immediate economic returns. Similarly, Personnel Expenditures, which also have a negative impact, indicate that an excessive dominance of bureaucratic spending tends to constrain fiscal space and reduce the overall efficiency of local financial management.

This study has several limitations that should be taken into account when interpreting the results. First, the measurement of financial performance using the regional financial independence ratio, in which PAD constitutes a primary component, creates an inherent mathematical connection between the dependent and independent variables. While this study provides a theoretical justification from an Institutional Theory perspective to treat PAD as

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an instrument of fiscal behavior, future research could benefit from using alternative measures of financial performance, such as efficiency, effectiveness, or growth ratios, to further validate these findings. Additionally, the sample was reduced from 108 to 99 observations due to outlier treatment conducted to satisfy the normality assumption, which may limit the representation of extreme fiscal conditions in certain regions.

Furthermore, the dataset used in this study contains observations across both regions and years, indicating a panel-data structure. However, the analysis employed pooled multiple linear regression rather than panel-data techniques. Consequently, unobserved regional characteristics and time-specific effects may not have been fully controlled. Future studies are encouraged to employ Fixed Effects Models (FEM) or Random Effects Models (REM) to obtain more robust estimates.

Lastly, as this study relies solely on secondary data obtained from Budget Realization Reports (LRA), future studies may integrate qualitative approaches, such as interviews with local government officials from BPKAD or Bappeda, to explore the political and managerial dynamics underlying budget allocation decisions and PAD optimization in West Java.

Based on the conclusions, practical recommendations for district and city governments in West Java Province include prioritizing strategies to intensify and expand local revenue (PAD) through the digitization of taxes and fees, as these have proven most significant in improving financial performance, as well as conducting rigorous evaluations of capital expenditure planning to ensure a focus on projects with direct economic impact (income-generating) and implementing rationalization or spending reviews of personnel expenditures to prevent them from reducing fiscal capacity for development. Future studies should broaden financial performance indicators beyond autonomy and efficiency ratios to include growth and solvency ratios, incorporate moderating variables such as the quality of corporate governance or local government size to examine whether negative effects of capital and personnel expenditures can be mitigated, and extend the observation period or conduct comparisons with provinces outside Java to enhance the generalizability of findings within the institutional theory framework.

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