



The Impact Of The Visa Exemption Policy On International Tourist Arrivals And Local Craft Trade In Indonesia

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ABSTRACT

The Visa Exemption Policy is a strategic measure aimed at increasing international tourist arrivals and fostering economic growth. This study examines the impact of the visa exemption policy on international tourist arrivals and local craft trade by utilizing panel data from 34 provinces in Indonesia over the period 2013–2023. The analysis employs a fixed effects model initially and an Ordinary Least Squares (OLS) approach with year-fixed effects subsequently. The regression results indicate that, on average, granting visa exemptions to an additional country leads to a 0.4% increase in international tourist arrivals. In the second model, a 1% increase in the number of international tourists contributes to a 0.492% rise in the Gross Regional Domestic Product (GRDP) of the local craft sector. The Sobel test further confirms that international tourist arrivals significantly mediate the relationship between the Visa Exemption Policy and local craft trade, with a z-value of 5.36. These findings suggest that the Visa Exemption Policy has a significant positive impact on local craft trade in Indonesia, albeit indirectly, through the mediation of increased international tourist arrivals.

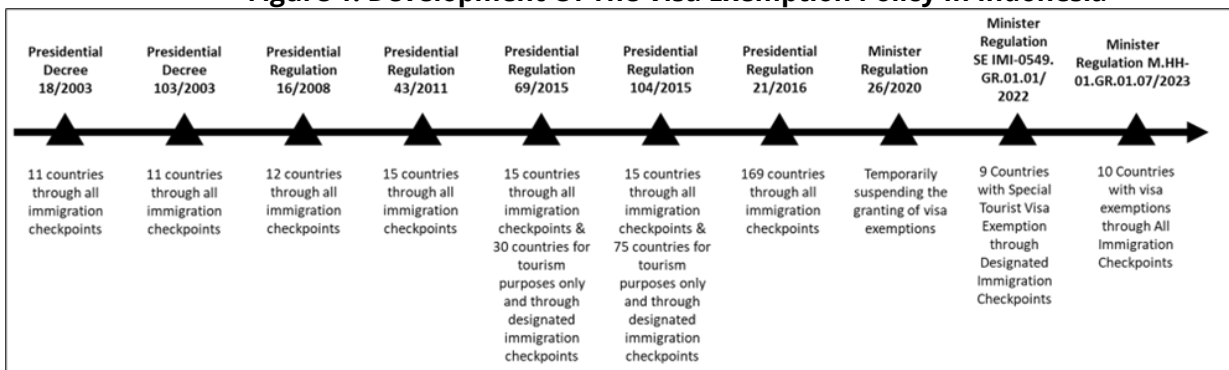
INTRODUCTION

The tourism sector is one of the key industries continuously promoted by the government to drive economic growth (Gu, 2024; Cortes-Jimenez & Pulina, 2010; Liu et al., 2018). According to Matthew et al. (2021), tourism plays a crucial role in increasing national income through foreign exchange earnings generated from tourist visits. Based on data from Bank Indonesia, processed by the Ministry of Tourism and Creative Economy, foreign exchange revenues from the tourism sector have shown an increasing trend, although a decline occurred due to the COVID-19 pandemic in 2020 and 2021. However, in 2023, tourism-related foreign exchange earnings rebounded, reaching USD 14 billion (Ministry of Tourism and Creative Economy, 2024).

Similarly, international tourist arrivals have generally followed an upward trend, although the COVID-19 outbreak led to a significant decline in 2020 and 2021. As the tourism sector began to recover post-pandemic, its growth potential became increasingly evident as a driver of economic recovery. In 2023, the number of international tourist arrivals nearly doubled compared to the previous year, with a total of 11.68 million foreign tourists visiting Indonesia (BPS, 2024).

One of the key instruments in attracting international tourists to a country is the visa exemption policy. By removing complex visa application procedures, this policy facilitates and increases international tourist arrivals (Meganingratna et al., 2021). In Indonesia, the visa exemption policy was first introduced in 1983 through Presidential Decree No. 15 of 1983. This regulation was subsequently revised and expanded, reaching its peak in 2016 with the issuance of Presidential Regulation No. 21 of 2016, which granted visa exemptions to 169 countries to boost the tourism sector and national economy. However, due to the COVID-19 pandemic from 2020 to 2022, the implementation of this policy was temporarily suspended. The following section provides an overview of the development of Indonesia's visa exemption policy.

Figure 1. Development Of The Visa Exemption Policy In Indonesia



Source: Prihartini & Yudhistira, 2023; Yudhistira et al., 2021; Ministry of Law and Human Rights, 2024

Several previous studies have indicated that visa exemption policies can have both positive and negative impacts on a country. In Indonesia, the visa exemption policy has influenced the tourism sector by increasing the number of foreign tourist arrivals by an average of 5%, and after one year of implementation, the growth rate reached 8% per year (Yudhistira et al., 2021). The visa exemption policy between South Korea and Japan has been proven to significantly boost tourist arrivals and economic revenue. In the first year, tourist arrivals increased by 12.1%, contributing US\$246 million to the economy. In the second year, tourist arrivals rose by 25%, generating US\$792 million in revenue (Lee et al., 2010). Furthermore, at the global level, 21% of the world's population was able to travel without a visa in 2023 (UNWTO, 2024).

On the other hand, visa exemption policies can also have negative consequences, such as increasing criminal activities, including human trafficking, illegal labor, and terrorism, due to the lack of control over the entry of foreign nationals (Santosa et al., 2022). A study by Prihartini & Yudhistira (2023) found that the visa exemption policy implemented between 2015 and 2019 contributed to an increase in immigration violations in Indonesia, with an average rise of 44.2%, consistent with previous research (Adinegara, 2018; Goto & Akai, 2017). However, based on a cost-benefit analysis conducted by Prihartini & Yudhistira (2023), the benefit-to-cost ratio of the visa exemption policy in Indonesia was found to be 2.4, indicating that the benefits derived from the policy outweigh the associated costs.

Given this context, this study aims to explore the impact of the visa exemption policy on international tourist arrivals and local craft trade in Indonesia. Previous research on the effects of visa exemption policies in Indonesia by Pujiharini & Ferika; Ichihashi (2016); Yudhistira et al.

(2021); Prihartini & Yudhistira (2023); and Malewa & Yudhistira (2024), as well as studies conducted in various other countries by Czaika & Neumayer (2017), Datta (2018), and Lee et al. (2010), have primarily examined the relationship between visa exemption policies and tourism. However, these studies have predominantly focused on the macroeconomic impacts of visa exemption policies, such as the increase in tourist arrivals, their contribution to government revenues, negative externalities, and their effects on international trade, without considering the microeconomic implications particularly how these policies influence the local craft sector, which is a vital component of the creative economy.

Based on this gap, the present study seeks to examine whether visa exemption policies have a significant impact on local craft trade in Indonesia. This research aims to provide new insights for policymakers and industry stakeholders regarding the importance of a comprehensive strategy that integrates tourism policies with the development of the creative economy in the craft sector. Through an in-depth analysis, this study aspires to clarify how visa exemption policies and the designation of priority tourism destinations can be optimized to support the growth of local craft trade while also identifying challenges that must be addressed to fully realize the economic potential of this sector.

LITERATURE REVIEW

Visa Exemption Policy and Its Impact on Tourism

Dwyer et al. (2020) emphasize that tourism decisions are influenced by economic factors such as income, relative prices, transportation costs, migration levels, natural disasters, and destination attractiveness. Additionally, Xu et al. (2023) and Xu, J. (2010) highlight that to enhance destination attractiveness, five fundamental elements in tourism should be improved: accessibility, attractions, accommodation, amenities, and activities. Among these components, one of the most effective ways to increase tourism appeal is by improving accessibility, which can be facilitated through the implementation of visa exemption policies.

Visa exemption policies are a strategic measure frequently adopted by developing countries to boost international tourist inflows (UNWTO, 2024; Neumayer, 2011). According to Czaika & Neumayer (2017), visa restrictions can reduce tourist flows by approximately 20%, as well as diminish opportunities for bilateral trade and investment. Studies in Indonesia indicate that visa exemption policies can increase tourist arrivals by 5% per month, with a more significant impact on non-traditional tourist destinations in the country (Yudhistira et al., 2021).

As international tourist arrivals increase, key tourism-related sectors such as hotels, restaurants, transportation, and tourist attractions experience higher revenue growth. For instance, the case of South Korea and Japan demonstrates that visa exemption policies led to an increase in tourism revenues of up to \$792 million in the second year of policy implementation (Lee et al., 2010). Other studies, such as those by Pujiharini, Ferika & Ichihashi (2016) and Artal-Tur et al. (2016), also support the argument that visa exemption policies have a positive impact on increasing international tourist arrivals.

The Relationship Between Tourism and Local Craft Trade in the Creative Economy Sector

Tourism is one of the key sectors driving a country's economic growth (Gu, 2024; Cortes-Jimenez & Pulina, 2010; Liu et al., 2018). The tourism sector generates a high multiplier effect, particularly in trade, hospitality, restaurants, and transportation (Sumastuti et al., 2021). Additionally, Rahmawati & Purwohandoyo (2019) found that tourism, particularly tourist arrivals, significantly impacts the marketing of local products such as wooden batik crafts, increases local community income, and creates an economic multiplier effect.

Similarly, Upadhyay (2020) discovered a significant positive correlation between craft products and tourist arrivals in Pokhara, Nepal. Studies by Tichaawa & Chamboko-Mpotaringa (2024) and Trupp et al. (2023) also found a positive correlation between tourism and local craft

products in tourism destinations such as sub-Saharan Africa and the Solomon Islands. Furthermore, Azharunnisa et al. (2024) highlighted that a sustainable approach to integrating tourism with local craft promotion can generate significant economic benefits for artisan communities in Puri, Odisha, India.

The craft industry, also known as the handicraft industry, is one of Indonesia's leading sub-sectors in the creative economy. According to the Ministry of Tourism and Creative Economy (2022), the craft sector is a branch of applied fine arts that merges artistic and design elements, rooted in either traditional heritage or contemporary ideas. The craft industry is also one of the three largest sub-sectors contributing to the Gross Domestic Product (GDP) of Indonesia's creative economy, alongside the culinary and fashion industries. This sub-sector has made a significant contribution to the national economy, particularly by creating employment opportunities and improving the welfare of local artisans across various regions in Indonesia (Ministry of Tourism and Creative Economy, 2024).

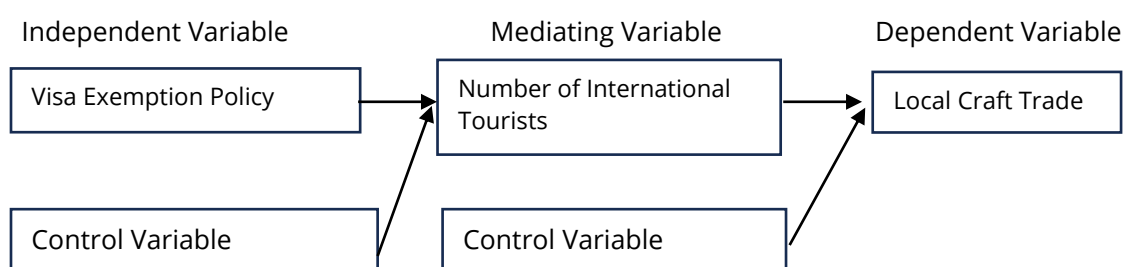
METHODS

This study employs secondary data sourced from various authoritative institutions, spanning the observation period from 2013 to 2023. The dataset comprises panel data involving all 34 provinces of Indonesia as the analytical units. The dataset utilized encompasses local craft trade figures, derived through the Gross Regional Domestic Product (GRDP) methodology, which categorizes economic outputs by specific business fields pertinent to the craft product industry. The GRDP figures by business sector are disseminated by the Central Statistics Agency (BPS).

Additionally, the categorization of craft product subcategories aligns with the Scope of Tourism and Creative Economy Activities as detailed in the 2020 Indonesian Standard Business Field Classification (KBLI) issued by the Ministry of Tourism and Creative Economy (Kemenparekraf). Furthermore, data concerning visa exemption policies are compiled from Presidential Decrees and legislation enacted by the Ministry of Law and Human Rights (Kemenkumham). Control variables include foreign tourist arrivals data sourced from BPS, provincial inflation figures from BPS and Bank Indonesia, and information on international airports and ports provided by the Ministry of Transportation. Data on natural disasters are acquired from the National Disaster Management Agency (BNPB), while policy data relating to the COVID-19 pandemic is obtained from Presidential Regulations.

This investigation delves into the indirect effects of visa exemption policies on local craft trade within Indonesia, utilizing the Fixed Effects Model (FEM) and Ordinary Least Squares (OLS) for estimations, following the empirical methodology outlined by Wijayanti & Khoirunurrofik (2022), Sutijah et al. (2020), and Gorondutse et al. (2014). The visa exemption policy, devised as a governmental tactic to enhance the attractiveness of tourism, is purported to bolster international tourist arrivals (Xu et al., 2023; Xu, J., 2010), which, in turn, is anticipated to positively influence local craft trade (Tichaawa & Chamboko-Mpotaringa, 2024; Trupp et al., 2023). The empirical model designed to analyze the indirect impact of visa exemption policy on local craft trade is illustrated as follows:

Figure 2. Illustration of the Empirical Research Model



Based on the illustration above, the first model is established to analyze the impact of the visa exemption policy on tourist arrivals, as follows:

$$\ln Tourist Arrivals_{it} = \alpha_0 + \alpha_1 VisaFree_{it} + \alpha_4 Inflation_{it} + IntAirport_{it} + \alpha_7 IntPort_{it} + \alpha_8 lnDisaster_{it} + \alpha_9 Covid_{it} + \gamma_i + \varepsilon_{it}$$

This study examines the impact of visa exemption policies on international tourist arrivals at the provincial level in Indonesia. The dependent variable, $\ln Tourist Arrivals_{it}$, represents the number of international tourist arrivals in province i at year t . The key independent variables include $VisaFree_{it}$, which indicates the number of countries granted visa exemptions for international tourists in accordance with prevailing regulations in province i at year t .

Several control variables are incorporated into the model to account for other factors influencing international tourist arrivals. $Inflation_{it}$ represents the inflation rate in province i at year t . Additionally, $IntAirport_{it}$ and $IntPort_{it}$ denote the number of international airports and seaports, respectively, in province i at year t . To account for external shocks, $lnDisaster_{it}$ measures the number of natural disasters occurring in province i at year t . Furthermore, $Covid_{it}$ is a dummy variable indicating whether the COVID-19 pandemic occurred (1 = pandemic year, 0 = non-pandemic year). The model also includes γ_i , which represents fixed effects for province, and ε_{it} , the error term capturing unobserved factors influencing the dependent variable.

Meanwhile, the second model is designed to examine the impact of international tourist arrivals on local craft trade. The regression model is formulated as follows:

$$\ln GRDPCraft_{it} = \beta_0 + \beta_1 \ln Tourist Arrivals_{it} + \beta_2 ProvTradeOpenness_{it} + \beta_3 RoadLength_{it} + \delta_t + \mu_{it}$$

The second model aims to analyze the impact of international tourist arrivals on local craft trade, measured through the Gross Regional Domestic Product (GRDP) approach in the craft industry sector. The dependent variable, $\ln GRDPCraft_{it}$, represents the GRDP of local craft trade, specifically derived from the manufacturing industry sub-sector related to craft production in province i at year t .

The key independent variable, $\ln Tourist Arrivals_{it}$, captures the number of international tourist arrivals in province i at year t , reflecting the potential influence of tourism on local craft trade. Additionally, $ProvTradeOpenness_{it}$ is included to measure the province trade openness ratio, calculated as the total exports and imports relative to the GRDP in province i at year t . This variable accounts for the extent to which a province is engaged in international trade, which may affect the craft industry. To control for infrastructure development, $\ln RoadLength_{it}$ is incorporated, representing the total road length in each province as an indicator of physical infrastructure quality in province i at year t . The model also includes δ_t , which represents year-fixed effects, accounting for unobserved time-specific factors affecting local craft trade, and μ_{it} , which denotes the error term capturing unobserved variations in the model.

In this model, the indirect effect of the visa exemption policy on local craft trade will be measured using the Sobel Test. Sobel, M.E. (1982) formulated this model to test the indirect effect between an independent variable (X) and a dependent variable (Y), which is mediated by a third variable (M). This test is used to determine whether the presence of the mediator (M) in the regression analysis significantly reduces the effect of variable X on Y. A similar approach was applied in the study by Wijayanti & Khoirunurrofik (2022), which examined the indirect impact of road corruption on income inequality. The Sobel Test formula used to calculate the indirect effect is as follows:

$$z = \frac{ab}{\sqrt{b^2SEa^2 + (a^2SEb^2)}}$$

In the Sobel Test, several key parameters are used to measure the significance of the indirect effect. The coefficient *a* represents the regression coefficient of the independent variable on the mediating variable, while *b* denotes the regression coefficient of the mediating variable on the dependent variable. The standard errors associated with these estimates are denoted as *SEa*, which is the standard error of estimation for the effect of the independent variable on the mediating variable, and *SEb*, which is the standard error of estimation for the effect of the mediating variable on the dependent variable. Z-score greater than 1.96 at a 5% significance level indicates that international tourist arrivals effectively mediate the relationship between the visa exemption policy with local craft trade. This result suggests that both the visa exemption policy have a significant impact on local craft trade in Indonesia, primarily through the increase in international tourist arrivals.

RESULTS

Descriptive Analysis

The first step in understanding each variable used in this study is to conduct a descriptive analysis. The explanation of the descriptive analysis results for each model is presented as follows:

Table 1. Summary Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
GRDPCraft*	374	13,539,289.00	28,215,635.00	24,200.00	150,200,000.00
VisaFree	374	74.09	75.53	0.00	169.00
TouristArrivals	374	314,369.49	1,147,154.70	10.00	11,637,486.00
Inflation	374	4.10%	2.50%	-0.20%	11.90%
ProvTradeOpenness	374	40.98%	43.16%	0.06%	307.82%
RoadLength	372	15,859.18	9,943.75	3,183.00	42,555.00
IntAirPort	374	0.84	0.76	0.00	3.00
IntPort	374	0.91	0.73	0.00	6.00
Disaster	374	98.14	169.97	1.00	1,358.00
Covid	374	0.27	0.45	0.00	1.00

* in million rupiahs

Table 1 presents the summary statistics for all variables used in this study. The average Gross Regional Domestic Product (GRDP) of the local craft sector (GRDPCraft) is IDR 13.54 trillion, with a standard deviation of IDR 28.22 trillion, indicating a substantial variation across provinces. The minimum GRDP of the local craft sector is IDR 24.2 billion, while the maximum value reaches

IDR 150.2 trillion, highlighting significant disparities in craft-related economic activities across regions. The number of international tourists (TouristArrivals) has an average of 311,847 tourists per province, with a minimum of 10 tourists and a maximum of 11.6 million tourists, suggesting that tourist arrivals are highly concentrated in certain key destinations.

First Model Regression Analysis Results

In the first model of the fixed effects regression analysis, the dependent variable Number of International Tourists (InTouristArrivals) is estimated based on the independent variable, Visa Exemption Policy (VisaFree), along with other control variables. The regression results are presented as follows:

Table 2. First Model Regression Results

Dependen Variable : InTouristArrivals		
Variable	Model	
	1	2
VisaFree	-0.008*** (0.001)	0.004*** (0.001)
Inflation		7.531*** (1.653)
IntAirPort		0.034 (0.366)
IntPort		0.041 0.072
InDisaster		-0.028 0.049
Covid		-1.157*** 0.099
Constant	8.844*** (0.250)	9.154 (0.799)
Observasi	371	371
Adj R-squared	0.8866	0.9392
Number of IDE	34	34

Robust standard error in parentheses ***p<0.01, **p<0.05, *p<0.1

Based on the regression results, Model 2 is selected as the best model due to its highest Adj R-squared value of 0.9392. This indicates that 93.92% of the variability in the dependent variable (InTouristArrivals) can be explained by the independent variables included in the model. The regression results show that the Visa Exemption Policy (VisaFree) has a coefficient of 0.004, which is statistically significant at the 1% level. This implies that an increase of one additional country receiving visa-free access to Indonesia leads to an average increase of 0.4% in international tourist arrivals.

This finding confirms that the visa exemption policy significantly drives international tourist flows to Indonesia. These results align with the existing literature, including studies by Lee et al. (2010), Pujiharini, Ferika & Ichihashi (2016), Artal-Tur et al. (2016), and Yudhistira et al. (2021), which demonstrate that visa exemption policies contribute significantly to the increase in international tourist arrivals in a country.

Second Model Regression Analysis Results

In the second model, the author estimates the impact of international tourist arrivals (InTouristArrivals) on the dependent variable, GRDP of the local craft sector (InGRDPCraft). The regression results are presented as follows:

Table 3. Second Model Regression Results

Dependen Variable : InGRDPCraft		
Variable	Model	
	1	2
InTouristArrivals	0.544*** (0.033)	0.492*** (0.031)
ProvTradeOpeness		0.440*** (0.165)
InRoadLength		0.895*** (0.109)
Constant	8.970*** (0.427)	0.893 (1.063)
Year Fixed-Effect	No	Yes
Observasi	371	371
Adj R-squared	0.414	0.507
Number of ID	34	34

Robust standard error in parentheses ***p<0.01, **p<0.05, *p<0.1

Based on the estimation results, Model 2 is selected as the best model, as it has the highest Adj R-squared value of 0.507, compared to Model 1, which has an Adj R-squared value of only 0.414. The higher Adjusted R-squared indicates that Model 2 provides a better explanation of the data variability, particularly after incorporating year fixed effects. These year fixed effects are crucial for capturing year-to-year variations, such as the impact of the COVID-19 pandemic, changes in national policies, or global economic fluctuations, which may uniformly affect craft trade across all provinces. Province fixed effects were not used in this model because the analysis focuses on measuring cross-provincial policy impacts, including variables that reflect fixed characteristics of each province, such as road length and trade openness. Using province fixed effects could eliminate important cross-provincial variations that are essential in explaining differences in craft trade contributions among regions. By omitting province fixed effects, the model retains geographical information and unique provincial characteristics, which are the main focus of this study.

The estimation results of Model 2 show that international tourist arrivals (InTouristArrivals) have a coefficient of 0.492, which is statistically significant at the 1% level. This indicates that a 1% increase in international tourist arrivals leads to a 0.492% increase in the GRDP of the local craft sector. These results confirm that the tourism sector significantly contributes to the growth of local craft trade, consistent with previous studies by Tichaawa & Chamboko-Mpotaringa (2024) and Trupp et al. (2023), which found a positive correlation between tourism and local craft products in tourism destinations. Additionally, Rahmawati & Purwohandoyo (2019) and Azharunnisa et al. (2024) state that tourism contributes to the growth of local craft trade and has a positive multiplier effect on the creative economy.

Overall, the second model regression results indicate that the tourism sector, trade openness, and road infrastructure have a significant impact on local craft trade. These findings support the hypothesis that the visa exemption policy plays an essential role in driving the

creative economy within the craft sector, although this study finds that its effect is mediated through international tourist arrivals (InTouristArrivals).

DISCUSSION

This study examines the indirect effect of the visa exemption policy on local craft trade using the Sobel Test method. The Sobel Test calculation is performed by incorporating the regression coefficients and standard errors from the two previous regression models into the Sobel Test equation. The Sobel Test result yields a z-score of 5.36, which is greater than the critical value of 1.96 at a 5% significance level. This confirms that international tourist arrivals serve as a mediating variable in the relationship between the visa exemption policy and local craft trade.

Therefore, based on this evidence, it can be concluded that the visa exemption policy has an indirect yet significant positive impact on local craft trade in Indonesia through international tourist arrivals as a mediating variable. This finding is in line with studies by Tichaawa & Chamboko-Mpotaringa (2024) and Trupp et al. (2023), which also found a positive correlation between tourism and local craft products. Additionally, Upadhyay (2020), in his study on Pokhara, Nepal, identified a significant correlation and dependency between craft products and tourist arrivals, further reinforcing the role of tourism in supporting the craft industry.

The next method to ensure the robustness and validity of the research findings is conducting a robustness check through regression analysis, where independent and control variables are gradually introduced into the model. The analysis results indicate that the impact of these variables on the dependent variable remains stable and consistent, both in terms of direction of the relationship and significance levels. This confirms the reliability and stability of the model used in this study.

CONCLUSION

Based on the regression results of the first model, it is shown that the Visa Exemption Policy (VisaFree) has a coefficient of 0.004, which is significant at the 1% level. This indicates that an increase by one country in the number of countries with visa exemption access to Indonesia can increase the number of international tourists by 0.4%. In the second model, the coefficient of InTouristArrivals is 0.492, which is also significant at the 1% level. This demonstrates that a 1% increase in the number of international tourists can enhance the GDP of the craft sector by 0.492%.

Furthermore, this research will examine the indirect effects of the Visa Exemption Policy on the Local Craft Trade using the Sobel Test calculation method. From the Sobel Test calculation, a z-value of 5.36 was obtained, which means that this value is greater than 1.96 with a significance level of 5%. This proves that the international tourist variable can mediate the relationship between the Visa Exemption Policy and the Local Craft Trade. Therefore, it can be indirectly concluded that the Visa Exemption Policy significantly positively affects the Local Craft Trade in Indonesia through the mediating variable of international tourists.

SUGGESTION

Based on the findings of the study, several strategic recommendations are suggested for the government, including the creation of promotional programs that integrate countries granted visa exemption for visits to Indonesia. This program could promote priority tourism destinations while simultaneously introducing Indonesia's premier craft products. This recommendation stems from research findings indicating that priority tourism destinations have not yet had a significant impact on the arrival of international tourists. Additionally, collaboration

among various stakeholders is essential, including central government agencies (such as the Ministry of Tourism, Ministry of Creative Economy, Ministry of Immigration and Civil Registration, Ministry of Trade, Ministry of Industry, and other relevant ministries/agencies) and local governments, to optimize policies that enhance tourism, namely the visa exemption policy and the establishment of priority tourism destination zones, in boosting the trade of local crafts.

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