

Can Government Spending and Foreign Capital Reduce Poverty? Evidence From ASEAN Countries

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ABSTRACT

This study aims to analyze the effects of government spending, foreign direct investment (FDI), labor, and economic growth on poverty levels in eight ASEAN countries during the period 2014–2023. Poverty in this study is proxied through household consumption, and the estimation model uses panel data regression with the Robust Least Squares (M-estimation) approach to address violations of classical assumptions such as residual non-normality. The estimation results show that government spending and economic growth have a positive and significant effect on household consumption, indicating their contribution to reducing poverty levels. In contrast, FDI and labor do not show a significant effect on household consumption. These findings indicate that the effectiveness of government spending and the quality of economic growth are key to poverty alleviation in the ASEAN region, while the benefits of FDI and increased labor require a more targeted and inclusive policy approach.

Keywords: ASEAN, FDI, Government Spending, Poverty, and Robust Least Squares.

INTRODUCTION

Poverty remains a pressing multidimensional challenge in many developing countries, including those in Southeast Asia. Although ASEAN countries have made significant progress in poverty reduction over the past few decades, income disparities and vulnerability to poverty remain crucial issues requiring serious attention. Promoting public welfare is one of the goals of national development. One of the success factors of development is the reduction of poverty (Nouvan et al., 2023). Poverty alleviation is an important agenda for a country to realize the welfare of its people so that poverty alleviation becomes an abroad and massive issue in implementing *Sustainable Development Goals (SDGs)* (Ambya et al., 2019). A comprehensive understanding of the factors influencing poverty levels is crucial for effective and sustainable policy formulation. Studies have identified a variety of macroeconomic and structural variables that play a role in determining poverty dynamics, but the complex interactions between these variables in the specific ASEAN context require further exploration.

Government spending plays a vital role in poverty alleviation efforts through the provision of public goods and services, infrastructure investment, and social transfer programs. Budget allocations for education, health, and social safety nets can directly improve the welfare of the poor and vulnerable (Salah et al., 2026). For example, government spending oriented towards increasing access to quality education can improve workforce capabilities and future employment opportunities. Similarly, investments in basic infrastructure such as roads and electricity can open market access for small producers and reduce transportation costs, which in turn can positively impact the incomes of poor households (Balasundaram, 2025). However, the effectiveness of government spending depends heavily on good governance, transparency, and accountability to prevent leakage and ensure benefits reach target groups.

Foreign Direct Investment (FDI) is often considered a driver of economic growth and job creation, indirectly contributing to poverty reduction. FDI brings capital, technology, managerial expertise, and access to global markets, all of which can boost productivity and innovation in recipient countries (Aloui et al., 2024). Sectors receiving FDI tend to experience increased production and export capacity, creating new job opportunities and increasing incomes. However, the impact of FDI on poverty is not always linear and positive. Several studies have shown that if FDI is concentrated in capital-intensive sectors that create fewer jobs or if there are inadequate mechanisms to transfer technology and expertise to the local workforce, its benefits for poverty reduction can be limited or even widen inequality (Umwali & Wei, 2026). Therefore, it is important to understand the characteristics of inward FDI and the supporting policies that can maximize its benefits for poverty reduction in ASEAN.

The availability and quality of labor are fundamental factors in determining poverty levels. An inclusive labor market, with decent wages and equal access to employment opportunities, is key to lifting people out of poverty (ILO, 2024). Increasing labor force participation, especially for vulnerable groups such as women and youth, can significantly reduce household poverty levels. Furthermore, investments in skills development and vocational education can increase labor productivity and competitiveness in global markets, which in turn promotes inclusive economic growth. Conversely, high unemployment, lack of relevant skills, or discrimination in the labor market can exacerbate poverty and inequality.

Economic growth is widely recognized as a key driver of poverty reduction. The "trickle-down effect" theory suggests that strong economic growth creates more jobs and incomes, ultimately benefiting the poor. However, the effectiveness of economic growth in reducing poverty depends heavily on the nature of the growth—whether it is inclusive and equitable or concentrated in a few sectors or individuals. Growth driven by labor-intensive and export-oriented sectors, which absorb large numbers of unskilled and semi-skilled workers, tends to

have a greater impact on poverty reduction. Conversely, non-inclusive growth can widen disparities and even exacerbate relative poverty (Akinci, 2011).

Increased government spending, foreign direct investment (FDI), and economic growth are generally considered to have a positive impact on poverty reduction in ASEAN countries. Government spending, particularly focused on social welfare, education, and health programs, can directly reduce the burden on the poor and improve their access to basic services. Research by Najmi et al. (2025) found that increased government social spending in Indonesia was negatively correlated with poverty rates, demonstrating the effectiveness of fiscal interventions in poverty alleviation. Similarly, FDI can create new jobs, transfer technology, and increase productivity, which in turn can promote inclusive economic growth and reduce poverty. A study by Bao et al. (2026) on Vietnam showed that FDI has a significant positive impact on poverty reduction through job creation and increased household income. Furthermore, strong and sustained economic growth often creates opportunities for the poor to participate in economic activities, earn income, and escape poverty. Rahman et al. (2026) in their research in several ASEAN countries emphasized that GDP per capita growth consistently correlated negatively with poverty levels, emphasizing the crucial role of economic growth in poverty alleviation efforts.

However, the relationship between these variables and poverty levels is not always linear or entirely positive, and can even have counterproductive effects if not managed properly. Government spending, for example, if inefficient or prone to corruption, may not effectively reach the poor. Anwar & Sari (2021), in their analysis of the effectiveness of poverty alleviation programs in several regions in the Philippines, highlighted that leakage and misuse of public funds can mitigate the positive impact of government spending. FDI, despite its significant potential, can also widen income inequality if the jobs created are predominantly in high-skilled sectors that are inaccessible to the poor, or if foreign companies do not adhere to fair labor standards. Aloui et al. (2024), found that although FDI increases economic growth, its benefits are not always distributed evenly and can even exacerbate income inequality in some regions. Furthermore, non-inclusive economic growth, which only benefits a few groups or sectors, will not significantly reduce poverty. In fact, economic growth that relies heavily on capital-intensive industries may not create enough jobs for the unskilled labor force, which is prevalent among the poor. Research by Aziz and Rahman (2023) in Malaysia shows that despite steady economic growth, absolute poverty in rural areas remains a serious challenge, highlighting the need for more targeted policies to ensure inclusive growth. Finally, labor issues, such as low minimum wages, lack of access to education and training, and discrimination, can also prevent the poor from taking advantage of existing economic opportunities, even amidst economic growth and investment. Setiawan and Putra (2024) suggest that despite increased employment in the manufacturing sector in several ASEAN countries, inadequate wages and poor working conditions remain significant barriers to improving the quality of life for poor workers.

While previous studies have identified government spending, foreign direct investment (FDI), labor, and economic growth as crucial factors in poverty alleviation efforts in ASEAN countries, a significant research gap exists regarding a deeper understanding of the complex interactions between these variables. The existing literature tends to analyze the impact of each variable separately or in limited combinations, as demonstrated by Najmi et al. (2025) on social spending, or Bao et al. (2026) on FDI. However, no research has comprehensively examined how these four factors influence, reinforce, or even inhibit each other in the specific

context of poverty reduction in ASEAN. For example, it remains poorly understood how synergies between government investment in education and FDI inflows can enhance the capacity of the local workforce to absorb economic benefits, or how specific characteristics of economic growth can optimize the positive impact of government spending and FDI on the poor.

The second research gap lies in identifying and testing the specific mechanisms and conditions of inclusiveness necessary for these variables to truly have a positive, equitable impact on poverty. Counterarguments in the cited literature (Aloui et al., 2024; Aziz and Rahman, 2023) consistently highlight that such positive impacts are not always linear and can even be counterproductive if governance is poor or if the benefits are not shared inclusively.

Therefore, further exploration of the prerequisite conditions or complementary policies that must be in place is needed. This includes an in-depth analysis of the type of governance that is most effective in ensuring transparency and accountability in public spending; regulations and FDI incentives that can foster quality job creation and widespread technology transfer; workforce skills development strategies that are responsive to market needs and changing economic structures; and the most inclusive economic growth model for the heterogeneous context of ASEAN countries. Future research should bridge this gap by examining the multidimensional interactions between variables and identifying specific pathways that lead to more effective and inclusive poverty reduction in the Southeast Asian region.

LITERATURE REVIEW

The literature review constitutes the theoretical foundation of a research article, as it situates the study within existing scholarly debates and identifies gaps that justify further investigation. A literature review is not merely a summary of prior studies but a critical synthesis of theories, empirical findings, and methodological approaches relevant to the research topic (Creswell S Creswell, 2018). Its primary purpose is to demonstrate mastery of existing knowledge, clarify what has been established, and explain how the current study contributes to unresolved issues (Hart, 2018). In development economics, poverty reduction is often linked to economic growth, public expenditure, and foreign investment. The influential argument that “growth is good for the poor” suggests a strong association between economic growth and poverty reduction (Ravallion, 2007). However, subsequent research emphasizes that the impact of growth depends on inclusiveness and income distribution (Ravallion, 2017). This debate underscores the importance of reviewing contrasting perspectives rather than relying on a single theoretical claim.

Government spending is theoretically justified within public finance frameworks, which argue that expenditure on education, health, and infrastructure improves welfare and reduces poverty (Salah et al., 2026). Empirical evidence supports this view. For instance, Najmi et al. (2025) find that social spending significantly reduces poverty when properly targeted. Nevertheless, governance quality remains crucial, as inefficiencies and leakages can undermine effectiveness. These findings suggest that the poverty impact of fiscal policy depends not only on the amount of spending but also on institutional quality. Foreign direct investment (FDI) is commonly viewed as a catalyst for employment, productivity, and technology transfer, which may contribute to poverty reduction (Aloui et al., 2024). Empirical evidence from Vietnam shows that FDI can positively influence household income under supportive domestic conditions (Bao et al., 2026). However, if FDI is concentrated in capital-intensive sectors, its benefits may bypass vulnerable groups and even widen inequality (Aloui et al., 2024). Thus, the poverty-reducing effect of FDI is conditional and context-dependent.

METHODS

This study will adopt a quantitative approach using panel data to analyze the influence government spending, foreign direct investment (FDI), employment, and economic growth on poverty levels in the ASEAN region. The use of panel data, which combines time-series and cross-section dimensions, was chosen because of its ability to identify country-specific effects and address the issue of unobserved heterogeneity between units (Baltagi, 2015). This allows for a more robust and informative analysis than using only time-series or cross-section data separately. The data used covers the period 2010 to 2023, with adjustments based on the availability of data from official sources such as the World Bank, the International Monetary Fund (IMF), and the ASEAN Secretariat. This study analyzes eight of the ten ASEAN countries: Brunei, Indonesia, Cambodia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam. Myanmar and Laos are excluded due to limited consistent and measurable poverty data within the study period.

Table 1. Operational Definition of Variables

No	Variable Name	Proxy	Unit	Data source
1	Poverty: Poverty is the inability to meet basic living needs due to insufficient income. (Sources: World Bank)	Household Consumption Expenditure	Percentage of GDP (%)	World Development Indicators
2	Government Spending: Government spending is public expenditure to provide goods, services, and development programs.	General Government Total Expenditure (% of GDP) [GE]	Percentage of GDP (%)	World Development Indicators
3	Foreign Direct Investment (FDI): FDI is foreign investment made to obtain lasting ownership and control in a business.	Foreign Direct Investment, net inflows (% of GDP) [FDI]	Percentage of GDP (%)	World Development Indicators
4	Labor: Labor is the workforce engaged in producing goods and services.	Labor force participation rate, total	Percentage of GDP (%)	World Development Indicators
5	Economic growth: Economic growth is the increase in a country's GDP per capita.	GDP per capita growth (annual %) [GDP]	Annual growth percentage (%)	World Development Indicators

To estimate the model, this study will use a panel data regression method. Three main approaches will be considered: Pooled Ordinary Least Squares (OLS), Fixed Effect Model (FEM), and Random Effect Model (REM). Pooled OLS will be used as the baseline model to examine the average relationship between variables without considering the specific characteristics of each country. However, given the potential heterogeneity among ASEAN countries, FEM and REM are

expected to be more relevant. FEM is suitable for use when there are unobserved variables correlated with the independent variable, thus controlling for unique characteristics of each country that do not change over time (Gujarati & Porter, 2009). Conversely, REM is more appropriate when country-specific effects are considered random variables uncorrelated with the predictors (Wooldridge, 2010). The selection of the best estimation model between FEM and REM will be determined using the Hausman Test. This test compares the consistency of the estimators of the two models, with the null hypothesis that the Random Effect Model is the most appropriate.

Regression Model

$$KM_{it} = \beta_0 + \beta_1 GVE_{it} + \beta_2 FDI_{it} + \beta_3 PTK_{it} + \beta_4 GWT_{it} + \epsilon_{it}$$

Where:

PE_{it} =Poverty

β_i =Constant

GVE_{it} = Government Expenditure

FDI_{it} =Foreign Direct Investment

RPN_{it} =Labor

GWT_{it} =Economic growth

ϵ_{it} =error term

Before interpreting the estimation results, a series of classical assumption tests will be performed to ensure the validity and reliability of the model. A multicollinearity test will be performed to detect high correlations between independent variables, which can lead to inefficient coefficient estimates and large standard errors. If detected, strategies such as variable transformation or variable deletion can be considered (Wooldridge, 2010). Next, a heteroscedasticity test will be performed to check whether the variance of the error terms is constant across observations. Violation of this assumption can lead to biased standard error estimates, which need to be addressed by using robust standard errors (Greene, 2018). Finally, an autocorrelation test will be performed to identify any correlations between error terms across time within each unit. If autocorrelation is detected, estimation methods such as FGLS (Feasible Generalized Least Squares) or robust standard errors adjusted for autocorrelation can be applied to obtain consistent and efficient estimates (Baltagi, 2015).

RESULTS

Model Significance Test Results

Table 2. Chow Test Results

Effects Test	Statistics	df	Prob.
Cross-section F	1.931352	(7.68)	0.0779
Cross-section Chi-square	14.50673	7	0.0429

Source: Eviews 9 Output, 2025

Table 2 shows that the Cross-section F Prob. value of 0.04 is smaller than the real level (α) of 5 percent, so H_0 is rejected and H_a is accepted so that it can be concluded that the Fixed Effect Model (FEM) method is better than the Common Effect Model (CEM) method for analyzing data in this study.

Table 3. Hausman Test Results

Test Summary	Chi-Sq. Statistic	Chi-Sq. df	Prob.
Random cross-section	6.916772	4	0.1404

Source: Eviews 9 Output, 2025

Table 5 shows that the p-value of 0.14 is greater than the significance level α of 5% (0.05), so it can be concluded that the random effect method is better to use than the fixed effect method in this study.

Table 4. Lm Test Results

	Cross-section	Time	Both
Breusch-Pagan	0.100309	0.205585	0.305894
	-0.7515	-0.6502	-0.5802

Source: Eviews 9 utput, 2025

Table 4 shows that the p-value of 0.14 is greater than the significance level α of 5% (0.05), so it can be concluded that the common effect method is better to use than the random effect method in this study. Based on the results of the Chow Test, Hausman Test and LM Test, the common effect is the best to use in this study.

Classical Assumption Test Results

Normality Test Results

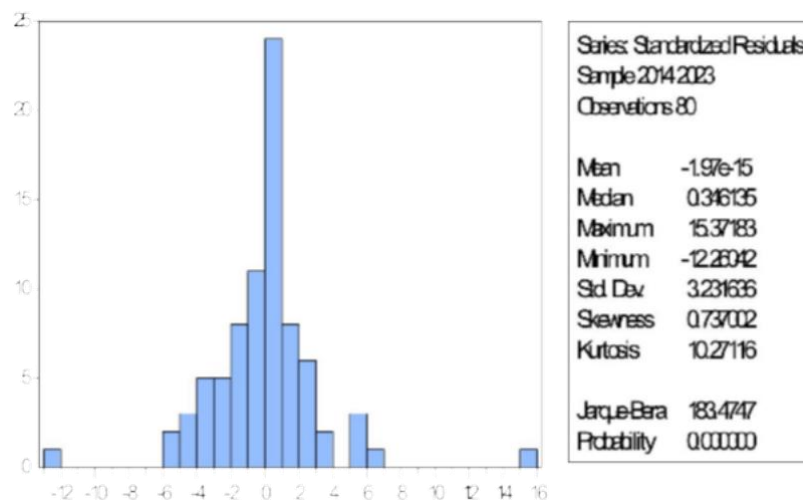


Figure 1. Normality Test Results

Source: Eviews 9 utput, 2025

Based on the Jarque-Bera test results, with a statistical value of 183.47 and a probability of 0.000000, it can be concluded that the residuals in the regression model are not statistically normally distributed. Therefore, it is recommended to use an estimation method that is robust to residual normality violations, such as regression with robust standard errors.

Multicollinearity Test Results

Table 5. Multicollinearity Test Results

Variables	GVE	FDI	PTK	GWT
GVE	1,000	-0.331	-0.553	-0.446
FDI	-0.331	1,000	0.269	0.066
PTK	-0.553	0.269	1,000	0.279
GWT	-0.446	0.066	0.279	1,000

Source: Eviews Processing, 2025

The analysis results show no signs of multicollinearity in the model. This is indicated by the Centered Variance Inflation Factor (VIF) values for all variables being below 10. As a general

rule of thumb, multicollinearity is considered present if the VIF value exceeds 10.

In this study, heteroscedasticity and autocorrelation tests were not performed separately because the regression model was estimated using robust standard errors. The use of robust standard errors is a common approach in panel data regression to address possible violations of the assumptions of homoscedasticity and absence of autocorrelation, without first having to perform formal classical tests. Robust standard errors automatically produce consistent variances and standard errors even when heteroscedasticity or autocorrelation are present in the model. According to (Wooldridge, 2010), in the context of panel or cross-section data, robust standard errors (including White or clustered standard errors) can provide valid and efficient estimates even when classical assumptions are violated. Therefore, this approach can be a valid alternative to manually performing classical assumption tests.

Regression Results

Based on the regression results with the common effect model, the following regression results are produced.

Table 6. Common Effect Model Regression Results

Variable	Coefficient	Std. Error	z-Statistic	Prob.
C	2.528623	3.618862	0.698734	0.4847
GVE	0.135709	0.060056	2.259707	0.0238
FDI	0.040234	0.031978	1.258171	0.2083
PTK	-0.03559	0.046429	-0.76662	0.4433
GWT	0.82528	0.07265	11.3596	0.0000
Robust Statistics				
R-squared	0.291192	Adjusted R-squared		0.253389
Rw-squared	0.697647	Adjust Rw-squared		0.697647
Rn-squared statistic	135.9268	Prob (Rn-squared stat.)		0
Non-robust Statistics				
Mean dependent variable	4,435	SD dependent var		4.322654
SE of regression	3.464978	Sum squared residual		900.4552

Source: Eviews 9 Output, 2025

Regression results using the Robust Least Squares method show that government expenditure (GVE) and economic growth (GWT) significantly influence the poverty rate, as proxied by household consumption. GVE has a positive coefficient of 0.136 with a p-value of 0.024, indicating that increased government expenditure tends to increase people's purchasing power and reduce poverty. Similarly, GWT has a coefficient of 0.825 and is highly significant (p-value 0.000), indicating that higher economic growth is strongly correlated with increased household consumption. Meanwhile, the FDI and PTK variables do not show a significant effect.

Overall, this model is significant based on the Rn-squared test (p-value 0.000), and the robust model has an Rw-squared value of 69.8%, indicating that the model is quite good at explaining variations in poverty after accounting for the presence of outliers and irregularities in the residual distribution. Therefore, the robust estimation method can be considered more appropriate than conventional OLS for this data.

Regression results using Robust Least Squares reveal important findings regarding the factors influencing poverty levels, as proxied by household consumption. This analysis reveals that government expenditure (GVE) and economic growth (GWT) have a significant influence on household consumption, indicating a positive impact on poverty alleviation efforts. The government expenditure (GVE) variable shows a positive coefficient of 0.136 with a p-value of 0.024. These results indicate that increased government spending tends to increase household consumption, which in turn can be interpreted as a reduction in poverty levels. The logic behind this finding is that government spending, through various programs such as subsidies, infrastructure investment, or improvements in public services, can directly or indirectly increase people's purchasing power. Increased purchasing power allows households to allocate more resources to the consumption of goods and services, thereby reducing vulnerability to poverty. This finding is consistent with several previous studies that have emphasized the important role of government intervention in poverty mitigation by improving economic welfare (Qi et al., 2026).

Economic growth (GWT) shows a coefficient of 0.825 and is highly significant (p-value 0.000). This high coefficient and very strong level of significance confirm that higher economic growth is strongly correlated with increased household consumption. In general, economic growth creates jobs, increases income, and stimulates overall economic activity. This mechanism provides more opportunities for households to earn income, which can then be allocated to consumption. The positive impact of economic growth on poverty reduction through increased household consumption has been widely documented in the economic literature (Nkukpornu et al., 2026). In contrast, foreign direct investment (FDI) and labor (CFT) variables do not show a statistically significant effect on poverty in this model. This could be because FDI has not been directed to labor-intensive sectors or has not had a direct impact on household income in the study countries. Meanwhile, the effect of labor indicates limitations in the quality or distribution of jobs that are insufficient to significantly alter poverty patterns

DISCUSSION

The findings of this study indicate that government expenditure and economic growth have a significant positive effect on household consumption, which is used as a proxy for poverty reduction in ASEAN countries. These results reinforce the theoretical argument that fiscal policy plays a crucial redistributive role in improving welfare outcomes. Public finance theory suggests that government spending on education, health, infrastructure, and social protection enhances human capital and expands access to economic opportunities (Salah et al., 2026). The positive and significant coefficient of government expenditure in this study supports empirical evidence that targeted public spending can directly increase household purchasing power and reduce vulnerability to poverty (Najmi et al., 2025).

However, the effectiveness of government spending cannot be separated from governance quality. Although fiscal expansion may stimulate household consumption, weak

institutional capacity, corruption, and inefficient allocation can limit its impact. Previous research emphasizes that leakage and mismanagement of public funds reduce the poverty-alleviating effects of fiscal programs (Hans & Prasetyia, 2025). Therefore, the positive relationship identified in this study suggests that, on average, ASEAN countries have managed to channel public expenditure in ways that support household welfare, but improvements in transparency and accountability remain essential to maximize impact.

Economic growth emerges as the most influential variable in the model, with a strong and highly significant coefficient. This finding aligns with the long-standing proposition that economic growth is a key driver of poverty reduction. Growth increases employment opportunities, raises income levels, and stimulates aggregate demand, thereby improving household consumption capacity. Nevertheless, the literature also warns that the poverty-reducing effect of growth depends on its inclusiveness (Ravallion, 2007). In the ASEAN context, sustained economic expansion has lifted millions out of poverty, yet disparities across regions and social groups persist (Asian Development Bank, 2023). Thus, while this study confirms the importance of growth, it also implies that policy emphasis should be placed on inclusive and labor-absorbing sectors to ensure equitable benefits.

In contrast, foreign direct investment (FDI) does not show a statistically significant effect on poverty in this study. This result reflects the mixed evidence found in prior research. On one hand, FDI is expected to generate employment, facilitate technology transfer, and enhance productivity (Aloui et al., 2024). On the other hand, its impact depends heavily on sectoral distribution and domestic absorptive capacity. If FDI is concentrated in capital-intensive industries or urban areas, the benefits may not reach low-income households and may even exacerbate inequality (Aloui et al., 2024). The non-significant result in this study suggests that, within the ASEAN sample, FDI inflows may not have been sufficiently directed toward labor-intensive sectors or accompanied by strong linkages with local enterprises.

Similarly, the labor force participation variable does not significantly affect household consumption in the regression model. This finding may indicate that employment quantity alone is insufficient to reduce poverty without improvements in job quality, wage levels, and working conditions. ILO (2024) emphasizes that decent work, rather than mere employment expansion, is essential for sustainable poverty reduction. Informal employment, underemployment, and low productivity jobs remain common in several ASEAN countries, limiting the income-generating potential of labor participation. Therefore, enhancing skills development and promoting productive employment are critical complementary strategies.

CONCLUSION

Based on the results of panel regression using the Robust Least Squares method, it can be concluded that government spending and economic growth have a significant influence on poverty levels in the ASEAN countries analyzed. Government spending directed at social programs and infrastructure has been shown to increase household consumption, which is an indicator of poverty reduction. Economic growth also plays a central role in increasing purchasing power and public welfare. Conversely, foreign direct investment and the number of workers did not show a significant influence on household consumption in this study. This indicates that FDI has not been optimally directed to

labor-intensive sectors, and that the quality and distribution of the workforce need to be improved to support more effective poverty alleviation.

ASEAN governments need to improve efficiency and accountability in managing public spending, particularly on poverty alleviation programs, education, and basic infrastructure development, which have a direct impact on improving public welfare. Furthermore, foreign direct investment (FDI) needs to be more strategically directed toward labor-intensive sectors that can absorb local labor, and be accompanied by incentive policies that encourage technology transfer and skills training for the community. Governments also need to develop workforce strengthening strategies by increasing access to vocational education, job skills training, and the creation of decent and productive jobs, particularly in the informal sector and rural areas. Sustainable economic growth should be encouraged to be more inclusive, ensuring that the benefits of such growth are felt by low-income and vulnerable groups, so that poverty alleviation efforts can be carried out more evenly and sustainably throughout the ASEAN region.

This study contributes theoretically by strengthening the evidence that government spending and economic growth are more effective in reducing poverty in ASEAN countries than FDI and labor force participation, highlighting the importance of inclusive growth and effective fiscal policy. From a policy perspective, the findings suggest that ASEAN governments should improve the efficiency of public spending, promote inclusive economic growth, direct FDI toward labor-intensive sectors, and strengthen workforce skills to achieve more sustainable and equitable poverty reduction.

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