



International Journal of Economics, Management and Social Science

Vol 9 No 1 March 2026

E-ISSN: 2614-3828 | P-ISSN: 2614-3887

Open Access: <https://journal.salewangang.net/ijemss/index>

The Role of Islamic Governance in Strengthening the Impact of Islamic Social Finance on Poverty Reduction: Evidence from ASEAN-4 Countries

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Article Info :

Received:

25/02/2026

Revised:

28/02/2026

Accepted:

09/03/2026

ABSTRACT (10 PT)

This study examines social budget allocation as a policy instrument for poverty alleviation in four ASEAN countries: Indonesia, the Philippines, Vietnam, and Thailand. From the perspective of Islamic Social Finance, social spending represents a redistributive mechanism aimed at improving social welfare and reducing poverty. This research also investigates the extent to which Islamic Governance, reflected in institutional quality through corruption control, transparency, and accountability, strengthens the effectiveness of social spending in reducing poverty. The study aims to analyze the empirical relationship between social budget allocation and poverty reduction while examining the moderating role of institutional governance. This study uses panel data from 2004–2023, selected purposively based on the characteristics of social development and governance in ASEAN-4 countries. Secondary data were obtained from the World Bank and analyzed using panel data regression. Based on the Lagrange Multiplier test, the Random Effect Model was selected as the most appropriate estimation model. The moderating role of institutional governance was examined using Moderated Regression Analysis. The results indicate that social spending significantly reduces poverty in ASEAN-4. However, its effectiveness depends on institutional governance quality. Low transparency and accountability weaken the positive impact of social spending. Strengthening governance is therefore essential to ensure effective poverty alleviation strategies.

Keywords : *Islamic Social Finance; Islamic Governance; Social Spending; Poverty Reduction; Institutional Governance*



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1. INTRODUCTION

Poverty remains one of the biggest development challenges in Southeast Asia, particularly in the four major ASEAN countries of Indonesia, Vietnam, Thailand, and the Philippines (often referred to as ASEAN-4). Although the region is often seen as the engine of economic growth in Southeast Asia, the reality is that millions of people still live in poverty. Data from the World Bank (2023) shows that around 9.4% of Indonesia's population still lives below the poverty line. This figure is even higher in the Philippines, reaching 18.1%. Thailand, which has achieved upper-middle-income country status, still has around 6.8% of its population living in poverty, while Vietnam has been relatively more successful in reducing poverty, with around 3.6% of its population living in extreme poverty. This situation highlights the gap between economic growth and equitable welfare distribution, where improved economic performance does not always lead to a significant reduction in poverty.

In the context of public policy, social budget allocation is one of the main instruments used by the state to reduce poverty through various programs such as social security, cash assistance, education subsidies, and health services. From the perspective of Islamic Social Finance, social

spending can be understood as a mechanism for redistributing welfare that aims to ensure a more equitable distribution of resources for vulnerable groups in society (Zain & Ali, 2017). Various empirical studies show that an increase in social spending has a positive correlation with a decrease in poverty rates, especially in developing countries. Huda et al. (2024) note that targeted social spending can improve the welfare of poor communities in Asia. However, the effectiveness of the social budget is not only determined by the amount of funds allocated, but also by the quality of distribution and efficiency of use (Ravenska et al., 2025). This shows that welfare-oriented fiscal policies require an effective management system so that the benefits are truly felt by the communities.

Within the ASEAN region itself, a number of social protection programs have been implemented to reduce poverty rates (Ong & Bista, 2015). Programs such as Conditional Cash Transfer in the Philippines and the Family Hope Program in Indonesia have proven to be effective in significantly reducing extreme poverty rates (Mamangan, 2018). However, the implementation of these programs still faces various challenges, particularly related to the uneven distribution of benefits and potential budget leakage (Piano, 2021). This condition shows that the success of social policies does not only depend on program design, but also on the quality of their implementation at the institutional level.

In this case, the quality of public governance is an important factor that determines the effectiveness of social policies (Petrova, 2021). Transparency and accountability are two main aspects of good governance (Bolívar et al., 2015). The theory of good governance emphasizes that transparency allows the public to gain access to fiscal information so that they can reduce the potential for corruption and budget misuse (Taiwo, 2025). Meanwhile, accountability ensures that public officials are responsible for the use of state resources (Kusmanto and Kuntadi, 2024). From an Islamic economic perspective, these principles are also in line with the concept of Islamic Governance, which emphasizes the management of public resources in a trustworthy, transparent, and responsible manner.

A number of studies show that transparency and accountability play an important role in improving the effectiveness of social policies. Aritonang and Trimurni (2024) emphasize that in Indonesia, accountability in the implementation of social assistance programs can strengthen public trust and increase beneficiary participation. Magno (2015) also shows that fiscal transparency in Vietnam and the Philippines contributes to the increased effectiveness of social protection programs. Conversely, research by Sabila and Atman (2025) finds that social policies that are not supported by strong transparency and accountability mechanisms tend to cause public dissatisfaction and weaken the legitimacy of the government.

Furthermore, various studies also show a close relationship between the quality of institutional governance and the effectiveness of social spending in reducing poverty. Putra (2019) asserts that social spending in Southeast Asia can only have an optimal impact if it is supported by strong fiscal governance. This means that large allocations of funds will not yield maximum results without an effective management system. In the context of fiscal transparency, Diep and Le (2025) provide empirical evidence that openness in public budget management in Vietnam and the Philippines contributes significantly to the success of poverty alleviation programs. This shows that transparency is an important prerequisite for the public to monitor budget use and ensure that social programs actually reach their target groups.

Meanwhile, Cook and Pincus (2014) emphasize that the success of poverty reduction programs in Southeast Asia is not only determined by the size of the budget allocation, but also by the extent to which the budget is managed transparently. Similarly, Cooray and Nam (2025) found that in Vietnam and the Philippines, good fiscal governance increased the effectiveness of social protection programs in reducing poverty rates.

Furthermore, other studies reinforce the relationship between governance and the effectiveness of social spending. Nugroho et al. (2021) highlight that fiscal accountability plays an important role in strengthening public trust and improving social policy outcomes. Research by Samudra and Purwati (2025) also confirms that in developing countries, weak governance causes social spending to have no significant impact on reducing inequality. Meanwhile, Febrian and Satria (2025) in a cross-country study of Asia noted differences in social spending performance in countries with strong institutions compared to those with weak governance.

In addition to transparency, accountability also plays an important role in improving the effectiveness of social policies. Antlöv and Wetterberg (2021) emphasize that in Indonesia, accountability in the implementation of social assistance programs not only strengthens policy outcomes but also increases the legitimacy of the government in the eyes of the public. This finding is in line with the research by Elberry et al., (2022), which found a positive relationship between fiscal transparency and public spending efficiency in developing countries. Transparent governance practices enable social spending to be more targeted and have a real impact on the poor. Furthermore, Perera and Lee (2013) show that institutional quality moderates the relationship between social spending and poverty reduction in Asia. Countries with better governance tend to achieve more significant poverty reduction impacts than countries with weak institutional quality.

Although various studies have shown the importance of the relationship between social budget allocation and institutional governance quality, there are still several gaps in the literature. First, some studies focus on the size of social spending allocations as the main factor in poverty reduction, while others emphasize the importance of governance quality as a determining factor. Second, existing cross-country studies are generally macro in nature and do not pay particular attention to specific regional contexts, especially the ASEAN-4 region, which has relatively similar social development characteristics. Third, in many studies, transparency and accountability are often combined in a broader governance index, so that studies that specifically highlight these two aspects are still relatively limited.

Based on these research gaps, this study aims to empirically analyze how transparency and accountability play a role in strengthening the relationship between social budget allocation and poverty reduction in ASEAN-4 countries. Within the framework of Islamic Social Finance and Islamic Governance, this study seeks to provide a more comprehensive perspective on how the quality of public governance can strengthen the effectiveness of welfare redistribution policies. Thus, this study is expected to not only enrich the academic literature on the relationship between fiscal policy and poverty alleviation, but also provide relevant policy recommendations for governments in the ASEAN region in designing more effective and sustainable poverty alleviation strategies.

2. RESEARCH METHODS

This study uses a quantitative approach with the aim of analyzing the empirical relationship between social budget allocation and poverty reduction in the ASEAN-4 countries, namely Indonesia, the Philippines, Vietnam, and Thailand. Within the conceptual framework of this study, social budget allocation is understood as a form of welfare redistribution policy implementation in line with the principles of Islamic Social Finance, while the quality of institutional governance as reflected in transparency, accountability, and corruption control is positioned as part of Islamic Governance practices in public policy management. This approach allows for a more comprehensive analysis of how social welfare-oriented fiscal policies can be more effective when supported by good institutional governance.

This study uses secondary data in the form of panel data covering the period from 2004 to 2023. The selection of this period is based on the availability of consistent data and the relevance of social policy and institutional governance developments in the ASEAN-4 countries. The sampling technique was purposive, taking into account the characteristics of economic development, social policy, and the relative comparability of institutional governance quality among the countries under study. The data used was obtained from various official sources, particularly from a database provided by the World Bank, which provides information on poverty indicators, social spending, and institutional governance indicators.

The main variables in this study consist of social budget allocation as an independent variable representing the state's welfare redistribution policy, poverty level as a dependent variable reflecting the outcome of social policy, and institutional governance as a moderating variable. Institutional governance is measured through indicators of transparency, accountability, and corruption control that are widely used in studies of public governance and economic development. In the context of this study, these indicators are used to assess the extent to which the quality of institutional governance can strengthen or weaken the effectiveness of social spending in reducing poverty levels.

Data analysis was conducted using panel data regression to identify the relationship between the research variables. The best estimation model was selected through a series of model selection

tests. Based on the results of the Lagrange Multiplier (LM) test, the Random Effect model was selected as the most appropriate estimation model to explain the variation in data between countries and between time periods. This model allows researchers to capture the heterogeneity of each country's characteristics that cannot be observed directly but have the potential to influence the relationship between research variables.

To test the role of institutional governance as a moderating variable, this study uses a Moderated Regression Analysis (MRA) approach. This approach is used to analyze how the interaction between social budget allocation and the quality of institutional governance affects poverty levels. Through this model, it can be determined whether institutional governance plays a role in strengthening or weakening the influence of social spending on poverty reduction. Thus, this analysis not only tests the direct influence of social budget allocation on poverty but also evaluates how the quality of public governance is an important factor in determining the effectiveness of poverty reduction policies in the ASEAN-4 countries.

The basic model used is panel regression, supplemented by Moderated Regression Analysis (MRA) for the existence of governance as a moderating variable. In general, the empirical model is formulated as follows:

$$\text{Basic Model: } Y_{it} = \alpha + \beta_1 AS_{it} + \epsilon_{it} \quad (1)$$

$$\text{Moderation Model } Y_{it} = \alpha + \beta_1 AS_{it} + \beta_2 TA_{it} + \beta_3 (AS_{it} \times TA_{it}) + \epsilon_{it} \quad (2)$$

where:

- Y : Poverty
- AS : Social Budget
- TA : Transparency and Accountability
- AS×TA : Interaction variable (Social Budget X Transparency and Accountability)
- I : Country
- t : Year
- α : Constant
- ϵ_{it} : Error term
- β_1 - β_{13} : Coefficient values

Based on the equation model above, the relationship between the variables in this study can be described as follows:

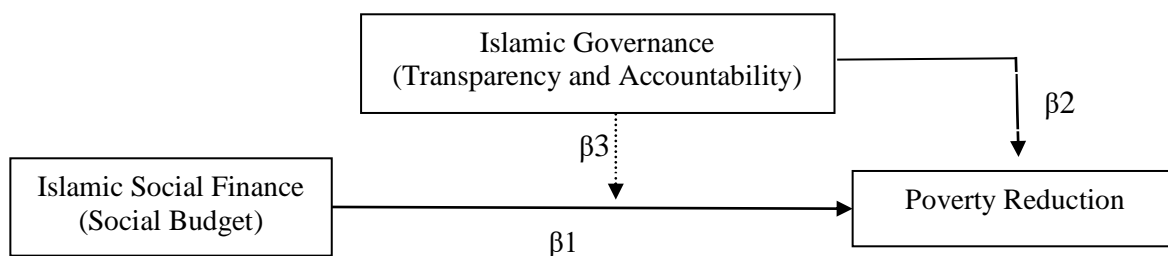


Figure 1 Research Framework

Description:

- > : Direct effect
-> : Moderation

3. RESULTS AND DISCUSSION

3.2 RESULTS

Descriptive Statistics

Descriptive statistics aim to provide an overview of the data obtained. Raw data is processed to make it easier to understand through summary figures (such as mean and standard deviation). The test results are as follows

Table 1. Descriptive Statistics

Variables	Observation	Mean	Std.Dev
Poverty	80	0.653930	0.205860
Location Social Budgeting	80	1.605052	0.293258
Transparency and accountability	80	1.609832	0.294806

Source: Data processed in 2025

Based on Table 1, the poverty variable has an average of 0.653930 with a standard deviation of 0.205860, indicating a relatively high level of poverty with moderate variation. The social budget allocation variable has an average of 1.605052 and a standard deviation of 0.293258, indicating that budget allocation is fairly stable across regions. Meanwhile, the transparency and accountability variable has an average of 1.609832 with a standard deviation of 0.294806, indicating a fairly good level of transparency and accountability with data variation that is almost the same as the social budget.

Model Selection Test

The model selection test aims to determine the most appropriate and suitable analysis model for the research data. Through this test, researchers can ensure that the model used is able to describe the relationship between variables more accurately, efficiently, and free from bias. Thus, the research results obtained are more valid and can be used as a basis for drawing conclusions.

Table 2. Model Selection Test

Test	Probability Value	Decision making	Description
Chow	0.0000	< 0.05 Fixed Effect > 0.05 Common Effect	Fixed Effect
Hausmant	0.8131	< 0.05 Fixed Effect > 0.05 Random Effect	Random Effect
LM	0.0000	< 0.05 Random Effect > 0.05 Common Effect	Random Effect

Source: Data processed in 2025

Based on Table 2, the Chow Test shows a probability of 0.0000 (< 0.05), indicating that the Fixed Effect model is more appropriate than the Common Effect model. However, the Hausman Test with a probability of 0.8131 (> 0.05) indicates that the Random Effect model is more appropriate. Therefore, continuing with the LM Test with a probability of 0.0000 (< 0.05), the model used is the Random Effect Model (REM). In accordance with the procedure, if REM does not require strict classical assumption testing because its estimation is based on GLS, which has overcome the problems of heteroscedasticity and autocorrelation. Therefore, in this study, it is not necessary to test classical assumptions (Musau et al., 2015).

Panel Data Regression Test

The panel data regression test aims to analyze the relationship between variables by utilizing data that has time series dimensions and individual or observation units (cross section) at the same time. The use of panel data allows for more accurate estimation results, reduces potential bias, and is able to capture the dynamics of changes over time and differences between individuals.

Table 3. Panel Data Regression Test

Variables	Coeff	Std.Error	t-Statistik	Prob
C	1.051308	0.152871	6.877074	0.0000
AS	-0.237111	0.048664	-4.872416	0.0001

Source: Data processed in 2025

Based on Table 3, the panel data regression test results show a constant of 1.051308 with a significance of $p < 0.05$. The social budget (AS) variable has a coefficient of -0.237111 with a probability of 0.0001, thus having a negative and significant effect on poverty. This means that an increase in social budget allocation (AS) actually reduces the poverty rate. Simply put, every 1 unit increase in the social budget is estimated to reduce poverty by 0.237111 units, assuming other variables remain constant.

Moderated Regression Analysis (MRA) Test

The MRA test aims to determine whether a moderating variable can strengthen or weaken the relationship between the independent and dependent variables. In other words, this test is used to see the role of moderating variables in influencing the direction and strength of the relationship between variables in the regression model.

Table 4. Moderated Regression Analysis (MRA) Test

Moderation	Variables	Coeff	Std.Error	t-Statistic	Prob
Moderation	C	-0.950544	0.779591	-1.219286	0.2377
	AS	1.565899	0.483611	3.237933	0.0043
	TA	1.306683	0.585106	2.233243	0.0378
	TA*AS	-1.174669	0.353299	-3.324860	0.0036

Source: Data processed in 2025

Based on Table 4, it shows that social budget allocation (AS) has a significant positive effect on poverty ($p = 0.0043$), and poverty (PK) is also significant ($p = 0.0378$). However, the PK*AS interaction has a coefficient of -1.174669 with $p = 0.0036$, which means that transparency and accountability weaken the effect of social budget allocation on poverty. Thus, although the social budget is effective in reducing poverty, its effectiveness will be reduced if it is not accompanied by good transparency and accountability.

3.2 DISCUSSION

Islamic Social Finance (Social Budget Allocation) and Poverty in ASEAN-4

Panel data regression results show that social budget allocation (SB) has a significant negative effect on poverty rates. This finding indicates that the greater the social budget allocation, the lower the poverty rate in ASEAN-4 countries, namely Indonesia, the Philippines, Vietnam, and Thailand. In other words, increased social spending has been proven to consistently reduce poverty rates, although its implementation varies between countries. Within the framework of Islamic Social Finance, this finding indicates that welfare redistribution policies through social budgets can serve as an important instrument in strengthening economic equality and improving community welfare.

Theoretically, these results are in line with the concept of the welfare state, which emphasizes the role of the state as a provider of a social safety net for society (Rostila, 2013). These findings also support the theory of resource distribution, which asserts that fiscal intervention through social budgets is an important instrument in reducing inequality and poverty (Huda et al. 2024; Ravenska et al. 2025). From an Islamic economic perspective, this redistributive function is also in line with the principles of Islamic Social Finance, which emphasizes the importance of fair wealth distribution in order to protect vulnerable groups in society (Dzulkepli & Barom, 2021). Thus, social budgets serve not only as economic instruments, but also as development strategies oriented towards distributive justice and improved social welfare.

Empirical evidence in the ASEAN region reinforces these findings. The Conditional Cash Transfer Program in the Philippines and the Family Hope Program in Indonesia have proven to be effective in reducing extreme poverty, especially among chronically poor households (Piano, 2021). This fact shows that a well-designed social budget can accelerate the process of poverty reduction. This consistency is also evident in various cross-country studies that confirm a significant relationship between social spending and improved community welfare. Putra (2019) emphasizes that social spending will yield more optimal results if it is directed at sectors that directly increase the productivity of poor groups, such as education and health. Thus, social spending not only functions as a mechanism for transferring funds, but also as a long-term investment in strengthening human capital.

However, the effectiveness of social budget allocation is not without challenges in its implementation (Van Domelen, 2002). First, the potential for budget leakage means that some of the program's benefits do not fully reach the target groups (Van Domelen, 2002). Second, the distribution of program benefits is often uneven, with urban areas tending to receive greater benefits than rural areas (Aaberge et al., 2010). Putra (2019), emphasize that the effectiveness of social spending is highly dependent on the quality of distribution and the efficiency of program implementation. This shows that increasing budget allocations without improving governance has the potential to reduce the

effectiveness of social policies. In this context, the principles of Islamic Governance are important as a control mechanism that emphasizes transparency, accountability, and the faithful management of public resources.

In the context of ASEAN-4, differences in fiscal capacity and development priorities also influence the composition of social spending in each country. Indonesia and Vietnam, for example, place greater emphasis on strengthening the education and health sectors as part of their human resource development strategies. Meanwhile, the Philippines and Thailand tend to pay greater attention to social security programs and subsidies for vulnerable groups. Although these policy approaches differ, the pattern that emerges is relatively uniform, namely that larger and more consistent social budget allocations have a significant impact on reducing poverty rates. Thus, social budget allocation can be seen as one of the key factors in poverty alleviation strategies in the ASEAN-4 countries. These findings reinforce the argument that social welfare-oriented fiscal policies are effective instruments in reducing social and economic inequality, although their success remains highly dependent on the quality of implementation and governance of these policies.

Strengthening Islamic Governance in Islamic Social Finance for Poverty in ASEAN-4

Based on the results of Moderated Regression Analysis (MRA), social budget allocation (SB) shows a significant positive coefficient on poverty levels. This finding indicates that an increase in social budget under certain conditions is actually correlated with an increase in poverty levels. These results reflect potential inefficiencies in social budget management, such as budget leakage, misdirected distribution, and ineffective use of resources. Without adequate oversight mechanisms, additional social budgets have the potential to cause misallocation or inappropriate allocation, and even create unproductive dependency among recipient groups.

Conversely, the interaction variable $SB \times G$ (Social Budget \times Governance) shows a significant negative coefficient. This result confirms that good governance, especially in terms of transparency and accountability, can reduce the counterproductive effects of social spending. In other words, social spending tends not to produce optimal results if it is carried out without the support of a strong governance system. However, when institutional governance is transparent and accountable, social budget allocations can be directed more effectively so that they truly contribute to poverty reduction. Within the framework of Islamic Governance, transparency and accountability serve as control mechanisms that ensure public budget management is carried out in a trustworthy, efficient, and targeted manner (Yunus, 2017).

Theoretically, these findings can be explained through the good governance theory framework, which emphasizes that fiscal policy will only yield optimal results if it is implemented in an institutional system that is transparent, accountable, and free from corrupt practices (Kusmanto and Kuntadi, 2024). Without strong institutional governance, social spending becomes vulnerable to budget leaks and irregularities in its implementation (Mogues & Erman, 2020). This condition can lead to a policy paradox, where an increase in budget allocation is followed by an increase in the risk of inefficiency, which ultimately reduces the effectiveness of poverty alleviation programs.

The results of this study are also in line with various findings in previous literature. Cook and Pincus (2014) emphasize that the size of social budget allocations in Southeast Asia does not automatically correlate with a decrease in poverty rates if the quality of institutional governance is weak. Nugroho et al. (2021) also highlight the importance of fiscal accountability as a prerequisite for social spending to increase public trust and produce optimal policy impacts. In fact, research by Sabila and Atman (2025) shows that low transparency in the management of social policies often triggers public dissatisfaction and weakens the legitimacy of the government.

In the context of the ASEAN-4 countries, these results also explain the variation in the effectiveness of social policies between countries. Indonesia and the Philippines, for example, still face various challenges in the management of social assistance, including potential corruption and leakage in program distribution, so that the positive impact of the social budget on poverty reduction is less than optimal. In contrast, Vietnam and Thailand show relatively better performance in terms of fiscal transparency, so that the social policies implemented tend to be more effective in reducing poverty (Cooray and Nam, 2025). Therefore, the negative moderation found in this study actually reflects the corrective mechanism function of institutional governance, which is to neutralize the

potential counterproductive impact of social spending while ensuring that budget allocations are used more efficiently and effectively.

Thus, institutional governance cannot be viewed merely as a complementary factor in social policy, but rather as a key determinant of the quality of policy implementation. Governance reform through increased fiscal transparency, strengthened bureaucratic accountability, and a more effective oversight system are important steps to ensure that social spending truly functions as a strategic instrument in reducing poverty in the ASEAN-4 region. These findings also reinforce arguments in previous literature (Elberry et al., 2022; Perera and Lee, 2013) that institutional quality moderates the relationship between social budgets and social outcomes. Without good governance, social budgets have the potential to be counterproductive, but with strong governance, social spending can function optimally as a real instrument for reducing poverty.

4. CONCLUSION

This study shows that social budget allocation in ASEAN-4 countries has an impact on poverty levels, but its effectiveness is greatly influenced by the quality of institutional governance. Panel data regression analysis shows that increased social spending contributes to a reduction in poverty levels. Within the framework of Islamic Social Finance, these findings show that welfare redistribution policies through social spending can be an important instrument in poverty alleviation efforts in the ASEAN region.

However, the results of the Moderated Regression Analysis (MRA) test show that this influence does not stand alone, but is highly dependent on the quality of institutional governance. Without good governance support, social spending has the potential to be ineffective and even fail to deliver the expected impact. The negative interaction between social budget allocation and governance quality indicates that weaknesses in transparency and accountability can reduce the effectiveness of social policies. From an Islamic Governance perspective, transparency and accountability serve as control mechanisms that ensure that social budgets are managed in a trustworthy, efficient, and targeted manner.

Theoretically, the findings of this study emphasize the importance of integrating welfare redistribution policies and institutional governance quality within the framework of social development. The success of social spending policies is determined not only by the size of the budget allocation, but also by how transparently and accountably the budget is managed. This reinforces the argument that good public governance is an important prerequisite for the effectiveness of poverty reduction policies.

In practical terms, the results of this study imply that governments in ASEAN-4 countries should not only increase social budget allocations, but also strengthen public governance systems, particularly in terms of fiscal transparency, accountability, and oversight mechanisms. These efforts are important to ensure that public resources truly reach poor communities and have a real impact on poverty reduction.

For further research, it is recommended to consider adding other variables that have the potential to influence the effectiveness of social policies, such as economic growth, income inequality, and bureaucratic quality. By including these variables, the analysis is expected to provide a more comprehensive picture of the factors that influence the success of poverty reduction strategies in the ASEAN region.

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