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The Effect of Village Funds on Poverty, Unemployment and Labor Force Participation Rate in Central Kalimantan Province 2020-2024

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ABSTRACT

Introduction/Main Objectives: This study evaluates the effectiveness of Village Funds on poverty rates, unemployment, and labor force participation in Central Kalimantan Province for the 2020–2024 period. **Background Problems:** The background is the importance of empirically assessing this national fiscal decentralization policy in promoting rural welfare. **Novelty:** The study's novelty lies in its comprehensive panel data analysis in specific regions with unique socio-economic characteristics. **Research Methods:** The research method used panel data regression analysis with the Chow and Hausman test on secondary data from 13 districts. **Finding/Results:** The results show that: (1) Village Funds have no significant effect on poverty reduction; (2) Village Funds have no significant effect on unemployment reduction; and (3) Village Funds actually have a significant negative effect on labor force participation. **Conclusion:** Village Fund allocation alone is insufficient to improve the welfare of rural communities in the study area. This implies the need for more targeted policy adjustments, such as shifting the focus from infrastructure development to community empowerment programs, improving governance, and involving local participation. The key message of the research is that the effectiveness of fiscal decentralization policies is determined more by the quality of absorption and program suitability, rather than simply the size of the budget.

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1. INTRODUCTION

The Village Fund (Dana Desa) represents one of Indonesia's most significant fiscal decentralization and rural development initiatives, institutionalized through Law No. 6 of 2014. With annual allocations exceeding tens of trillions of rupiah from the national budget, its primary mandates are to accelerate rural infrastructure development, reduce poverty, stimulate local economies, and enhance public service delivery at the village level (Ministry of Finance, 2017). This substantial and sustained fiscal transfer is predicated on the assumption that local governments and communities are best positioned to identify and address their specific development needs, thereby promoting more equitable and inclusive growth beyond urban centers.

Despite its scale and strategic importance, there remains a critical gap between the program's ambitious objectives and robust empirical evidence of its socioeconomic impact at the regional level. Aggregate national data often mask significant geographical disparities in implementation capacity, local governance, and contextual challenges. Central Kalimantan Province serves as a poignant case study. Characterized by a dispersed population, pockets of high rural poverty, and uneven development progress as illustrated by the Village Development Index (IDM), the province's socioeconomic landscape presents a complex environment in which to assess the fund's effectiveness (Ministry of Villages, 2024). While funds have been consistently disbursed, it is unclear whether these financial inflows have successfully translated into tangible improvements in key welfare indicators for the local population.

This study is therefore motivated by a pressing need to move beyond policy rhetoric and budgetary figures to conduct a rigorous, data-driven evaluation. The core problem we address is the uncertainty regarding the causal efficacy of the Village Fund allocation in achieving its fundamental goals within a specific, challenging regional context. Consequently, this research is designed to answer the following pivotal question: Does the allocation of the Village Fund have a statistically significant effect on reducing poverty and unemployment, and on increasing labor force participation, across the districts of Central Kalimantan from 2020 to 2024?

To answer this question, we bridge empirical and methodological gaps in the extant literature. Theoretically, we draw upon frameworks of fiscal decentralization, Nurkse's theory of the vicious circle of poverty, and Lewis's model of labor transition. Methodologically, we contribute by employing a panel data regression analysis, which allows us to control for unobserved heterogeneity across districts and isolate the temporal effect of the fund. This approach provides a more nuanced and reliable assessment than cross-sectional or purely descriptive studies.

The objectives of this study are threefold: (1) to quantitatively analyze the influence of Village Fund disbursements on the district-level poverty rate; (2) to examine its impact on the open unemployment rate; and (3) to assess its relationship with the labor force participation rate (LFPR) in Central Kalimantan. Our findings, derived from a balanced panel of 13 districts over a five-year period, reveal a nuanced reality: the Village Fund demonstrated no significant effect on poverty or unemployment reduction and was associated with a slight but significant decrease in labor force participation. These results underscore that substantial fiscal allocation alone is an insufficient condition for development, highlighting the critical importance of program quality, local governance, and strategic targeting. This introduction sets the stage for a detailed literature review on rural development and fiscal policy, followed by a comprehensive presentation of our methodology, empirical results, and their implications for theory and policy.

2. LITERATURE REVIEW

The efficacy of fiscal decentralization as a tool for equitable regional development and poverty alleviation is a central theme in development economics. This review synthesizes theoretical and empirical literature across three interconnected strands to establish the foundation for our research question and hypotheses:

the theory and impact of fiscal decentralization, the multifaceted challenges of rural poverty, and the dynamics of local labor markets.

2.1 Fiscal Decentralization and Rural Development

The theoretical premise of fiscal decentralization, as articulated by Oates (1972) in his "Decentralization Theorem," posits that local governments possess superior information about constituent preferences, enabling more efficient and responsive public good provision compared to a centralized authority (Miyazaki, 2025). The Village Fund policy aligns with this logic, intending to empower villages as primary agents of their development (Madyan et al., 2020). Empirically, studies on similar intergovernmental transfers yield mixed results. Research in India on the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) suggests that well-targeted, employment-linked fiscal programs can significantly reduce poverty (Das, 2016). However, a critical gap identified in the literature is the mediating role of local institutional capacity. Lele (2019) argue that the benefits of decentralization are contingent upon robust local governance, accountability, and absorptive capacity factors often weak in remote rural settings like those in Papua, Papua Barat, Aceh and Yogyakarta, the same thing also applies in Kalimantan. Much of the existing analysis on Indonesia's Village Fund remains macroeconomic or descriptive, lacking rigorous econometric assessment of its micro-level socioeconomic outcomes in specific geographic contexts, thus creating a gap this study addresses.

2.2 The Persistent Challenge of Rural Poverty

To conceptualize the intended outcome of the Village Fund, we engage with theories of poverty traps. Nurkse's (1953) "vicious circle of poverty" provides a foundational framework, illustrating how low income leads to low savings, inadequate investment, and sustained low productivity a cycle particularly relevant to isolated rural economies (Kraay & McKenzie, 2014). Breaking this cycle requires a coordinated "big push" in investment across multiple sectors (Bateman et al., 2009). The Village Fund is, in essence, designed to be such an exogenous injection of capital. Yet, the literature cautions that capital infusion alone is insufficient. Banerjee and Duflo (2007), in their seminal work on the economic lives of the poor, demonstrate that the poor face a complex bundle of constraints including lack of information, behavioral biases, and poor access to markets that blunt the impact of simple cash or capital transfers. This suggests that for the Village Fund to succeed, its programs must be intricately designed to address these specific local constraints, a nuance often missing in one-size-fits-all transfer policies.

2.3 Labor Market Dynamics in Developing Regions

The fund's objectives of reducing unemployment and increasing labor force participation intersect with theories of structural transformation. Lewis's (1954) dual-sector model posits that development involves transferring surplus labor from low-productivity traditional sectors (e.g., subsistence agriculture) to higher-productivity modern sectors. Public works and local enterprise development, common uses of village funds, aim to catalyze this transition. However, the success of such interventions hinges on the quality of created opportunities. Acosta & Marcenaro (2024) distinguishes between "good" and "bad" jobs in developing economies, noting that informal, low-productivity work does little to sustainably raise incomes or alter economic structures. Furthermore, a low or declining labor force participation rate (LFPR) can signal discouragement among workers or increased engagement in education (Litzinger & Dunn, 2015; Krueger, 2017). Therefore, analyzing the fund's impact requires moving beyond simple unemployment metrics to examine the quality of employment and the drivers of LFPR changes, a linkage not thoroughly explored in evaluations of Indonesia's village policy to date.

2.4 Synthesizing the Gap and Forming Hypotheses

This review reveals a critical intersection of ideas. While fiscal decentralization is a theoretically sound mechanism, its success in alleviating poverty is mediated by local institutional capacity and the design of interventions that target specific market failures and behavioral constraints (Ali Khan, 2013; Digdowiseiso, 2022). Furthermore, the impact on labor markets is not automatic but depends on the nature of the economic activities stimulated.

Prior studies on the Village Fund have often been broad, policy-focused, or lacking in causal identification. This leaves a clear gap: a need for a localized, econometrically robust study that tests the fundamental assumptions linking fiscal transfers to poverty reduction and labor market outcomes. Grounded in the theories and empirical findings discussed, we derive the following testable hypotheses for Central Kalimantan:

H1: The allocation of the Village Fund has a significant negative effect on the district-level poverty rate.

H2: The allocation of the Village Fund has a significant negative effect on the district-level open unemployment rate.

H3: The allocation of the Village Fund has a significant positive effect on the district-level labor force participation rate (LFPR).

This study will test these hypotheses, thereby contributing empirical evidence to the theoretical debates on decentralization, poverty traps, and rural labor market transformation.

3. METHOD, DATA, AND ANALYSIS

3.1 Model and Variable Definitions

This study uses a Panel Data Regression Model with the following equations:

1. Poverty Rate (Y1it): Measured based on the percentage of poor people in the village.

2. Unemployment Rate (Y2it): Measured based on the percentage of open unemployment in the village.

3. Labor Force Participation Rate (Y3it): Measured based on the percentage of the working-age population actively involved in economic activities.

The independent variable is the Village Fund (X1it), which is measured based on the logarithm of the Village Fund allocation.

3.2 Data Type and Source

The data used is secondary data from the Central Statistics Agency (BPS) of Central Kalimantan Province and the Ministry of Finance. The data covers the period 2020-2024 and covers 13 districts in Central Kalimantan.

3.3 Data Analysis & Processing Techniques

The analysis technique used is panel data regression. Hypothesis testing is performed using statistical tests such as the Chow test and the Hausman test to determine the best model. The analysis was performed using the E-Views 10 application. The empirical specification of the panel regression model is follow:

1. Poverty Model

$Poverty\text{it} = \alpha_1 + \beta_1 \ln(VF\text{it}) + \mu\text{i} + \epsilon_1\text{it}$ ………………………………………………. (3.1)

2. Unemployment Model

$Unemployment\text{it} = \alpha_2 + \beta_2 \ln(VF\text{it}) + \mu\text{i} + \epsilon_2\text{it}$ ……………………………………… (3.2)

3. Labor Force Participation Rates (LFPR) Model

$LFPR\text{it} = \alpha_3 + \beta_3 \ln(VF\text{it}) + \mu\text{i} + \epsilon_3\text{it}$ ………..……………………………………. (3.3)

Where;

Yit	= Dependen variable in district *i* at year *t*
*VF*it	= Village Fund Allocation
Ln (*VF*it)	= Natural logarithm of Village Fund
μit	= Unobserved district – specific effect
€it	= error term
i	= 1, 2, . . ., 13 districts
t	= 2020, . . ., 2024

4. RESULT AND DISCUSSION

4.1. The Impact of Village Funds on Poverty Rates

Poverty is a major focus for the government because it is a challenging issue to address. Poverty can arise from circumstances that force someone into poverty, such as economic crises and hedonistic lifestyles.

Table 1. Panel Data Regression Results: The Effect of Village Funds on Poverty Rates

Dependent Variable: Y1
Method: Panel EGLS (Cross-section random effects)
Date: 06/18/25 Time: 05:12
Sample: 2020 2024
Periods included: 5
Cross-sections included: 13
Total panel (balanced) observations: 65
Swamy and Arora estimator of component variances

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	5.113352	0.471025	10.85580	0.0000
X	0.006164	0.047275	0.130391	0.8967
Effects Specification				
			S.D.	Rho
Cross-section random			1.073429	0.9474
Idiosyncratic random			0.253017	0.0526
Weighted Statistics				
R-squared	0.000264	Mean dependent var		0.541011
Adjusted R-squared	-0.015605	S.D. dependent var		0.253980
S.E. of regression	0.255954	Sum squared resid		4.127276
F-statistic	0.016614	Durbin-Watson stat		1.132676
Prob(F-statistic)	0.897851			
Unweighted Statistics				
R-squared	0.012867	Mean dependent var		5.160769
Sum squared resid	78.42150	Durbin-Watson stat		0.059612

Source: Processed data.

The analysis results indicate that the best method to test the impact of Village Funds on poverty rates is the Random Effects Method. The panel data regression results can be written as:

Y1it = 5.113352 + 0.0061631it + εit

This indicates that although Village Funds have increased and the direction of the effect is positive (+0.006), their effect on poverty reduction is not yet significant (p=0.896). If all variables are set to 0, the average poverty rate is 5.11%. This means that for every 1% increase in Village Funds, the poverty rate actually increases by 0.006. Factors such as the low quality of education and the Village Fund's focus on infrastructure may be contributing factors.

Regional economic development is a collaborative process between local governments and communities to manage resources, collaborate with the private sector, create jobs, and ultimately drive economic growth

(Burhanuddin et al., 2024). Local governments have four key roles: entrepreneurs, coordinators, facilitators, and initiators. Poverty is cyclical (a vicious cycle) and requires major interventions (a big push) to break it, such as massive investment, soft skills development, and population growth control. Village funds are expected to be a big push to stimulate development through local government investment (Karim et al., 2024).

4.2 The Impact of Village Funds on Unemployment Rates

Employment opportunities are the number of individuals who can be absorbed into work at an MSME, agency, or CV, or even a company/PT. The expansion of employment opportunities is influenced by the following factors: population and workforce growth, economic growth, and related policies (Yacoub, 2012).

Table 2. Panel Data Regression Results: The Effect of Village Funds on the Unemployment Rate

Dependent Variable: Y2
Method: Panel EGLS (Cross-section random effects)
Date: 06/18/25 Time: 05:25
Sample: 2020 2024
Periods included: 5
Cross-sections included: 13
Total panel (balanced) observations: 65
Swamy and Arora estimator of component variances

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	3.912717	0.621170	6.298945	0.0000
X	0.001647	0.071182	0.023135	0.9816

Effects Specification

	S.D.	Rho
Cross-section random	1.033911	0.8120
Idiosyncratic random	0.497414	0.1880

Weighted Statistics

R-squared	0.000008	Mean dependent var	0.825668
Adjusted R-squared	-0.015864	S.D. dependent var	0.493521
S.E. of regression	0.497421	Sum squared resid	15.58791
F-statistic	0.000535	Durbin-Watson stat	1.507236
Prob(F-statistic)	0.981616		

Unweighted Statistics

R-squared	0.001623	Mean dependent var	3.925385
Sum squared resid	76.79057	Durbin-Watson stat	0.305958

Source: Processed data.

The results of this panel data regression test indicate that the best method researchers can use to analyze the influence of village funds on poverty levels is a random effects model. The panel data regression results can be written as follows:

Y2it = 3.912717 + 0.0016472it + ε2it

This indicates that although Village Funds increased and the direction of the effect was positive (+0.001), their effect on reducing the unemployment rate was not significant (p=0.982). If all variables were set to 0, the unemployment rate would be 3.91%. This means that for every 1% increase in Village Funds, the unemployment rate actually increased by 0.001%. A positive coefficient indicates a unidirectional relationship (unexpected), but it is not statistically significant. Village Funds were not proven to reduce unemployment in this model. Regional differences are more dominant in influencing the TPT than temporal factors.

An excess of workers in one sector can create an opportunity to stimulate growth in other sectors. In Central Kalimantan, the relatively small population can be a serious problem, as this study found that funds had no significant impact on the unemployment rate in villages. Other factors contributing to the insignificant impact of village funds could be that village development programs have not prioritized community participation, and policies regarding expanding employment opportunities have not been effectively implemented. It is hoped that the four priorities for village fund use, such as village pre-schools (Prukades), reservoir construction, development of village-owned enterprises (BUMDes), and village sports facilities, will absorb the labor force within the villages themselves (Rammohan & Tohari, 2023; Karim et al., 2024; Haeril et al., 2025).

4.3 The Influence of Village Funds on Labor Force Participation Rates (LFPR)

Humans are the primary production factor that determines the prosperity of a country or nation (Morozova et al., 2024; Bykova et al., 2024). The foundation of economic growth lies in the availability of efficient human resources (Sa et al., 2024). To maintain economic growth, human capital accumulation must be balanced with economic growth (Apergis et al., 2022). Effective distribution of human resources is a crucial prerequisite for the economic success of a country or nation.

The LFPR (Employment Allowance) is a measure that provides a clear picture of the ratio between the labor force and the workforce (Litzinger & Dunn, 2015). The workforce consists of the labor force and the non-labor force. The labor force is the portion of the workforce actually engaged in productive activities, namely producing goods and services (Sullivan, 2019). Meanwhile, the non-labor force is the portion of the workforce that is unemployed or seeking work; in other words, the portion of the workforce not involved in production activities. This study shows that village funds have no significant, but positive, effect on LFPR in villages in Central Kalimantan province.

Table 3. Panel Data Regression Results: The Effect of Village Funds on Labor Force Participation Rates

Dependent Variable: Y3
Method: Panel EGLS (Cross-section random effects)
Date: 06/18/25 Time: 05:36
Sample: 2020 2024
Periods included: 5
Cross-sections included: 13
Total panel (balanced) observations: 65
Swamy and Arora estimator of component variances

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	73.62034	1.970372	37.36367	0.0000
X	-0.545044	0.232389	-2.345399	0.0222
Effects Specification				
			S.D.	Rho
Cross-section random			2.834699	0.6427
Idiosyncratic random			2.113414	0.3573
Weighted Statistics				
R-squared	0.080660	Mean dependent var	21.96015	
Adjusted R-squared	0.066068	S.D. dependent var	2.181631	
S.E. of regression	2.108332	Sum squared resid	280.0389	
F-statistic	5.527451	Durbin-Watson stat	1.827423	
Prob(F-statistic)	0.021863			
Unweighted Statistics				
R-squared	0.138584	Mean dependent var	69.42769	
Sum squared resid	729.4359	Durbin-Watson stat	0.701569	

Source: Processed data.

The results of this panel data regression test indicate that the best method researchers can use to test the effect of village funds on the labor force participation rate is a random effects model. The panel data regression results can be written as follows:

Y3it = 73.6203 - 0.5450443it + ε3it

This indicates that although the Village Fund increased and the direction of the effect was negative (-0.545), its effect on the decline in the labor force participation rate was significant (p=0.0222). If all variables are equal to 0, the labor force participation rate is 73.62%. The coefficient is negative and statistically (β = -0.545, $p < 0.05$), indicating that a 1% increase in Village Funds is associated with a 0.55 percentage point decrease in labor force participation. The negative and statistically significant effect of Village Funds on labor force participation rate may be interpreted through the lens of Human Capital Theory (Becker, 1964; Mincer, 1974). According to this framework, individuals allocate time between schooling and labor market participation based on expected future returns (Rammohan & Tohari, 2023). If Village Funds indirectly improve access to education, through infrastructure, school facilities, or household income support, households may rationally choose to increase school enrollment rather than immediate labor participation (Khusaini et al., 2023; Karim et al., 2024). In this context, a temporary decline in labor force participation does not necessarily reflect labor market deterioration, but rather than an intertemporal investment decision in human capital accumulation. Therefore, the observed decline in LFPR may represent a structural adjustment toward long-term productivity gains rather than short-term economic stagnation. Supporting data from BPS indicates that school participation rates in Central Kalimantan remain relatively high among younger cohorts. If Village Funds allocations reduce household liquidity constraints, parents may prioritize schooling over child labor participation. This substitution effect aligns with standard household labor supply models, where income effects reduce labor supply when basic needs are secured (Kosec et al., 2023). A negative coefficient indicates a non-unidirectional relationship, but it is not significant. Village funds were not proven to reduce unemployment in this model. Regional differences are more dominant in influencing the TPT than temporal factors.

Other factors indicate that the results of this study are insignificant. A positive and insignificant LFPR value does not always indicate something positive. One of the variables that determines the number of people not in the labor force is the number of students. According to the Central Kalimantan Statistics Agency (BPS) in 2022, based on completed education data for the Central Kalimantan Province, the average number of people without a diploma was 66.9%, with 54.9% having completed elementary school/degree, 71.16% having completed junior high school/degree, and 86.56% having completed high school/degree. Specifically, in Central Kalimantan, the expected length of schooling percentage is 12.75%, the average length of schooling is 8.54%, and the Human Development Index is 73.41%. This means that the expected length of schooling in Central Kalimantan Province is still relatively low. A low LFPR with a positive relationship can indicate the need for improvements in education so that children in rural areas who have dropped out of school can return to school.

5. CONCLUSION AND SUGGESTION

This study concludes that Village Funds are ineffective in reducing poverty and unemployment in Central Kalimantan during the 2020–2024 period, and are even negatively related to labor force participation. These findings confirm that the success of fiscal decentralization is not automatically achieved through fund allocation alone, but is highly dependent on the quality of governance, program suitability, and absorption capacity at the village level.

This study provides critical empirical evidence against the theoretical assumption that direct capital injections alleviate poverty. The policy implication is the need to shift the focus from physical infrastructure development to community-based empowerment programs, skills training, and strengthening accountability and participatory planning. Evidence from India's MGNREGA Program (Das, 2016) demonstrates that employment-linked fiscal transfers can significantly reduce rural poverty when explicitly tied to labor-intensive public works. This suggests that redesigning Village Fund programs toward productive employment generation, rather than predominantly infrastructure-focused spending, may enhance labor market outcomes.

The main limitation lies in the nature of secondary data, which cannot reveal the causal mechanisms behind these results. A key limitation of this study is the absence of governance quality indicators at the village level. Previous literature (Lele, 2019) emphasizes that fiscal decentralization outcomes depend critically on local institutional capacity and accountability mechanisms. Without controlling for governance variation, the estimated impact of Village Funds may mask heterogeneous effectiveness across districts. Future research is recommended to use a mixed-methods approach, expand the scope of the study area comparatively, and include mediator variables such as the quality of village governance and school enrollment rates for more in-depth analysis.

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Declaration of AI and AI-assisted technologies in the writing process (if author[s] utilize AI)

In preparing this manuscript, the author used DeepSeek AI as an aid for proofreading, grammar checking, and sentence condensation in several sections of the background and conclusion. After using this service, the author independently reviewed, edited, and developed the content. The author is fully responsible for the content, data analysis, interpretation of the results, and all statements contained in this publication.

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