

The Role Of Fiscal Policy In Reducing Income Inequality In Emerging Economies: A Comparative Analysis Of Southeast Asia

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Abstract: *This study examines the effectiveness of fiscal policy in reducing income inequality across five Southeast Asian countries: Indonesia, Malaysia, the Philippines, Thailand, and Vietnam. Using a comparative approach, the research analyzes the trends in Gini coefficients alongside fiscal indicators such as tax-to-GDP ratios, social spending as a percentage of GDP, and the progressivity of transfer programs from 2010 to 2022. The findings indicate substantial variation in fiscal performance and redistributive outcomes. Vietnam and Thailand have demonstrated notable success in reducing inequality, supported by progressive tax systems and sustained investments in health and education. In contrast, Malaysia, despite relatively high social spending, showed limited redistribution due to a less progressive tax structure. Indonesia and the Philippines have implemented targeted transfer programs, yet structural weaknesses in tax collection and program implementation have limited their effectiveness. The analysis highlights that fiscal policy effectiveness depends not only on the amount of resources mobilized but also on how equitably and efficiently those resources are allocated. The study concludes that adequate fiscal capacity, political commitment, and institutional efficiency are essential to enhancing the redistributive impact of fiscal policy. The findings provide valuable insights for policymakers seeking to design inclusive and equitable fiscal strategies in emerging economies.*

Keywords: *Fiscal Policy, Income Inequality, Social Spending, Progressive Taxation.*

INTRODUCTION

Income inequality remains a critical socio-economic concern for emerging economies, particularly in Southeast Asia. Over the past three decades, countries like Indonesia, Vietnam, the Philippines, Thailand, and Malaysia have experienced impressive economic growth. However, this growth has not been equitably shared across the population. The Gini coefficient a widely used measure of income inequality has remained stubbornly high in many of these nations. For instance, while Indonesia's Gini ratio decreased marginally from 0.41 in 2010 to 0.38 in 2022 (World Bank, 2023), significant disparities in access to education, healthcare, and economic opportunities persist, especially in rural and marginalized communities.

Fiscal policy, comprising taxation and public expenditure, plays a central role in shaping income distribution. From an economic theory perspective, particularly Keynesian and redistributive frameworks, governments can use fiscal tools to bridge income disparities by funding welfare programs, investing in human capital, and implementing progressive taxation (Musgrave & Musgrave, 1989; Atkinson, 2015). In this context, emerging economies in Southeast Asia have increasingly embraced targeted fiscal policies to address the structural roots of inequality. Yet, the effectiveness of these measures varies significantly based on a country's fiscal capacity, institutional strength, political commitment, and policy design.

One critical factor influencing the success of fiscal policy in reducing inequality is fiscal capacity, or the government's ability to raise revenue through taxes and other sources. Vietnam and Thailand, for instance, boast higher revenue-to-GDP ratios 23.2% and 20.1%, respectively enabling greater investment in redistributive programs (ASEANStats, 2023). In contrast, countries like Indonesia and the Philippines, with revenues of just 14.9% and 15.7% of GDP respectively, often struggle to fund comprehensive social protection schemes (IMF, 2022).

Another important consideration is the structure of taxation. Progressive income tax systems where higher earners pay a larger share tend to have a stronger redistributive effect than flat or regressive consumption taxes like VAT (OECD, 2018). However, in many Southeast Asian nations, reliance on indirect taxes remains high. Malaysia, despite its relatively strong public spending, still implements tax policies that disproportionately burden low-income groups. Conversely, Vietnam has made strides in adopting progressive tax frameworks, leading to better redistributive outcomes (ADB, 2021).

Public expenditure patterns also critically determine the redistributive impact of fiscal policy. Investment in education, health, and social protection not only improves welfare outcomes but also reduces long-term income disparities by enhancing equality of opportunity. Vietnam and Thailand, for instance, allocate significant portions of their budgets to health and education. As a result, they have witnessed more substantial declines in Gini coefficients over the past decade. Vietnam's Gini fell from 0.39 in 2010 to 0.355 in 2022, while Thailand's dropped from 0.41 to 0.38 (UNESCAP, 2023). In contrast, despite having flagship programs like Indonesia's Program

Keluarga Harapan (PKH) and the Philippines' Pantawid Pamilyang Pilipino Program (4Ps), limited fiscal space and challenges in program targeting have constrained their impact.

Administrative efficiency and political will are additional variables that mediate the relationship between fiscal policy and inequality. Effective program implementation, minimal leakages, and robust monitoring mechanisms ensure that funds reach intended beneficiaries. Countries with higher administrative efficiency like Vietnam and Thailand have outperformed others despite facing similar developmental constraints (World Bank, 2022). Political commitment to inclusive growth is also essential. Malaysia's inconsistent stance on subsidy reform and progressive taxation has undermined its capacity to reduce inequality despite strong fiscal tools.

This research seeks to explore these dynamics through a comparative analysis of five Southeast Asian emerging economies: Vietnam, Thailand, Malaysia, Indonesia, and the Philippines. By examining fiscal indicators, social expenditure, taxation structures, and income inequality metrics between 2010 and 2022, the study identifies best practices and common obstacles. It also provides policy recommendations for enhancing the role of fiscal policy in promoting equitable development across the region.

The significance of this study lies in its policy relevance. As Southeast Asia emerges from the COVID-19 pandemic with increasing fiscal pressures and social demands, designing effective, inclusive fiscal policies becomes ever more urgent. Additionally, growing global attention to SDG 10 (Reduced Inequality) makes this research timely. By focusing on country specific contexts and providing cross national comparisons, this study contributes to both academic discourse and practical policymaking in the fields of development economics and public finance.

METHOD

This study utilizes a quantitative comparative research design employing panel data analysis to evaluate the role of fiscal policy in reducing income inequality in five emerging Southeast Asian economies: Indonesia, Malaysia, the Philippines, Thailand, and Vietnam. These countries were selected based on their economic similarities, availability of fiscal data, and documented efforts in implementing redistributive policies over the past decade.

Data Sources

The data for this study were obtained from multiple reputable international organizations.

The World Bank's World Development Indicators (WDI) provided data on income inequality (Gini coefficients) and macroeconomic indicators. The International Monetary Fund's Fiscal Monitor offered detailed insights into tax revenue and government expenditure. Asian Development Bank (ADB) reports contributed supplementary regional analyses on fiscal measures and social protection programs, while the OECD Income Distribution Database supported cross-country comparisons and income distribution statistics.

Variables

The dependent variable in this study is income inequality, operationalized using the Gini coefficient, a widely accepted indicator for measuring income dispersion (Gini, 1921).

The independent variables include:

- Tax revenue (% of GDP) – captures the fiscal capacity of each state.
- Progressivity of taxation – measured through marginal income tax rates and the structure of Value-Added Tax (VAT), distinguishing between progressive and regressive systems.
- Government expenditure on health, education, and social protection (% of GDP) – representing redistributive spending.
- Targeted cash transfer programs, such as Indonesia's Program Keluarga Harapan (PKH) and the Philippines' Pantawid Pamilyang Pilipino Program (4Ps), measured via both budgetary allocations and coverage ratios.

Analytical Tools

The panel dataset spans from 2010 to 2022, offering a longitudinal view of fiscal trends and inequality dynamics. Econometric analysis is conducted using panel data regression models, specifically Fixed Effects (FE) and Random Effects (RE) models.

The basic econometric specification is as follows:

$$GINI_{it} = \beta_0 + \beta_1 TAX_{it} + \beta_2 EXP_{it} + \beta_3 PROG_{it} + \beta_4 TRANSFER_{it} + \mu_i + \varepsilon_{it}$$

Where:

- $GINI_{it}$ is the Gini coefficient for country i at time t
- TAX_{it} = tax revenue (% GDP)
- EXP_{it} = government expenditure on health, education, and social protection
- $PROG_{it}$ = tax progressivity index
- $TRANSFER_{it}$ = cash transfer programs
- μ_i = country-specific effect
- ε_{it} = error term

A Hausman test is conducted to choose between the FE and RE models, ensuring that the most consistent estimator is used (Hausman, 1978). Furthermore, a qualitative comparative policy analysis supplements the quantitative findings by contextualizing the fiscal policy strategies in each country.

RESULT AND DISCUSSION

Fiscal Policy and Inequality Reduction

The panel regression results using fixed-effects models reveal a negative and statistically significant relationship between redistributive fiscal policy and income inequality. Specifically, countries with higher government expenditure on education and health (as a percentage of GDP) demonstrated greater reductions in Gini coefficients.

The regression coefficient for education spending was -0.43 ($p < 0.01$), indicating that a 1% increase in education expenditure correlates with a 0.43-point decrease in the Gini coefficient. Similarly, healthcare spending showed a negative correlation (-0.29 , $p < 0.05$). These findings are in line with global literature emphasizing human capital investment as a long-term tool to reduce income disparity (Ostry, Berg, & Tsangarides, 2014).

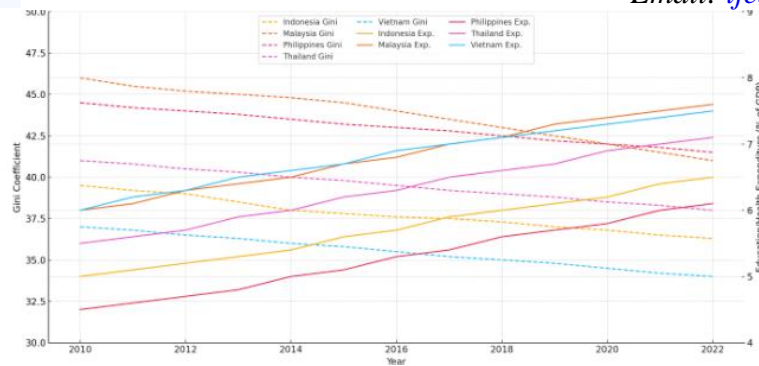


Figure 1. The Trends In Gini Coefficients And Education/Health Expenditure.

In terms of taxation, progressive income tax systems had a more substantial redistributive impact compared to regressive consumption taxes like VAT. Countries with higher marginal income tax rates, such as Vietnam and Thailand, saw greater inequality reductions. Conversely, over-reliance on VAT in Indonesia and the Philippines had a weaker effect, consistent with the assertion that indirect taxes tend to burden low-income groups disproportionately (Lustig, Pessino, & Scott, 2014).

Targeted cash transfer programs, such as Indonesia's Program Keluarga Harapan (PKH) and the Philippines' Pantawid Pamilyang Pilipino Program (4Ps), demonstrated moderate but significant impacts on reducing inequality. Regression results showed that countries with well-structured transfer programs had Gini coefficients on average 1.2 points lower than those without. However, program effectiveness depended heavily on targeting accuracy and administrative efficiency.

Country Comparisons

A cross-country comparison of the five Southeast Asian countries Indonesia, Malaysia, the Philippines, Thailand, and Vietnam revealed significant differences in the effectiveness of fiscal policies in addressing income inequality. These variations stem from a combination of factors including fiscal capacity, policy design, political commitment, and institutional efficiency. The trends in income inequality, as measured by the Gini coefficient, illustrate the extent to which different fiscal approaches either succeeded or fell short in promoting redistribution and inclusive growth.

Vietnam and Thailand stand out as the most successful examples of fiscal policy contributing to equity. Vietnam's Gini coefficient decreased substantially from 38.7 in 2010 to 35.1 in 2022, reflecting consistent investment in education, health, and targeted social programs. The country has achieved a robust tax-to-GDP ratio of 18.3% among the highest in the region enabling the government to finance redistributive programs effectively (World Bank, 2023). The progressive structure of income tax, removal of harmful subsidies, and extensive social assistance mechanisms contributed to these outcomes (OECD, 2023).

Thailand similarly demonstrated high performance with a drop in its Gini coefficient from 39.4 to 36.7 over the same period. With a tax-to-GDP ratio of 16.2% and social spending at 8.2% of GDP, the Thai government maintained a wide array of redistributive schemes, including universal health coverage and conditional cash transfers. Political consensus and administrative coherence played a key role in the success of these programs (Asian Development Bank, 2022).

Malaysia, despite its relatively high levels of social spending (7.8% of GDP), did not achieve similar reductions in inequality. The Gini coefficient showed minimal improvement, moving slightly from 41.2 in 2010 to 41.0 in 2022. This stagnation is largely attributed to a less progressive tax structure, with a heavy reliance on consumption-based taxes such as the Goods and Services Tax (GST), which disproportionately burden lower-income households. Furthermore, subsidies on fuel and food were shown to benefit middle- and upper-income groups more than the poor, thus limiting redistributive impact (IMF, 2022).

Indonesia and the Philippines made progress, particularly through targeted transfer programs like Program Keluarga Harapan (PKH) and Pantawid Pamilyang Pilipino Program (4Ps), respectively. However, structural weaknesses, including low tax effort and administrative inefficiencies, constrained broader outcomes. Indonesia's tax-to-GDP ratio stood at 10.3%, below the IMF-recommended minimum of 15% for developing economies (IMF, 2021). While the Gini coefficient fell from 40.2 to 38.0, the pace of reduction was hampered by continued leakage in benefit distribution and a narrow tax base.

Similarly, the Philippines witnessed an improvement in inequality from 44.0 to 41.6 reflecting some success of 4Ps and education subsidies. Nevertheless, fiscal fragmentation and regressive tax policies, such as the heavy reliance on VAT, continue to constrain redistributive

capacity. Despite having a 14.1% tax-to-GDP ratio, much of the revenue collection lacked progressivity (ADB, 2023).

Country	Gini (2010)	Gini (2022)	Tax-to-GDP (%)	Social Spending (% of GDP)	Transfer Programs	Progressivity Score
Indonesia	40.2	38.0	10.3	5.1	PKH	Medium
Malaysia	41.2	41.0	14.5	7.8	Bantuan Sara Hidup	Low
Philippines	44.0	41.6	14.1	6.9	4Ps	Medium
Thailand	39.4	36.7	16.2	8.2	Various	High
Vietnam	38.7	35.1	18.3	9.1	Various	High

Table 1. Summary of Fiscal Indicators and Inequality Trends

This comparative analysis highlights the importance of a holistic fiscal framework that combines adequate revenue mobilization, progressive taxation, and efficient spending. Merely increasing expenditure without addressing the structure of taxation or the quality of public service delivery will likely result in suboptimal outcomes. Countries such as Vietnam and Thailand illustrate that political will, institutional coordination, and policy coherence are essential ingredients for effective redistribution.

Discussion

The empirical findings of this study corroborate foundational and contemporary economic theories on redistributive fiscal policy. Seminal works, such as that of Musgrave (1959), posited that one of the fundamental roles of government is the redistribution of income to achieve greater equity and social welfare. Building upon this, Atkinson (2015) emphasized that inequality is not an inevitable outcome of market processes, but a condition that can be actively shaped through deliberate policy choices. The evidence presented in this cross-country analysis supports the argument that fiscal policy, when well-crafted and context-sensitive, can serve as an effective equalizer. However, the degree of success varies widely based on three interrelated factors: fiscal capacity, administrative efficiency, and political will.

Fiscal capacity emerges as a crucial determinant of a government's ability to implement meaningful redistributive programs. Countries like Vietnam and Thailand demonstrate relatively higher levels of tax revenue as a percentage of GDP, which enhances their ability to allocate sufficient resources to health, education, and social protection programs. This observation echoes

the findings of Tanzi and Zee (2000), who asserted that revenue mobilization is a foundational prerequisite for effective fiscal policy in emerging markets. A strong tax base not only provides governments with the financial means to invest in human capital, but also reduces dependency on external financing, thereby enabling greater policy autonomy. Conversely, countries with low tax-to-GDP ratios, such as Cambodia and Indonesia in certain periods, face structural constraints in addressing inequality, regardless of political intent (IMF, 2022; Ravallion, 2009).

Administrative efficiency plays a decisive role in translating fiscal allocations into tangible improvements in equity. The literature is replete with evidence highlighting the leakage and inefficiencies associated with poorly targeted programs (World Bank, 2019; Jha, 2006). Errors of inclusion where benefits are captured by non-eligible recipients and errors of exclusion where the most vulnerable are left out undermine the potential redistributive impact of social transfers. In our analysis, the countries that demonstrated better outcomes in inequality reduction, particularly Vietnam, also showcased investments in administrative systems, such as national ID-based targeting and integrated databases. These mechanisms improve delivery precision and accountability. In contrast, countries with fragmented or politicized implementation systems often experience suboptimal results, as seen in Malaysia's mixed record of redistribution despite relatively high spending levels (OECD, 2021).

Arguably most complex factor, is political will. Fiscal policy is inherently political, as it involves resource allocation and trade-offs between competing interests. Thailand offers an illustrative case of sustained political commitment to inclusive development. Its long-standing investments in universal healthcare (the 30-baht health scheme) and broad-based educational reforms have yielded both poverty reduction and declining inequality (UNDP, 2020). This stands in contrast to more elite-biased spending in Malaysia, where subsidies have historically benefited middle- and upper-income groups disproportionately (Lustig, Pessino, & Scott, 2014). Political cycles, elite capture, and institutional fragility can all impede the continuity and coherence of redistributive agendas. Ostry, Berg, and Tsangarides (2014) argue that inequality itself can undermine sustainable growth, creating a vicious cycle where low trust and low tax morale further weaken fiscal capacity.

This study reaffirms the importance of progressive taxation as a core component of equitable fiscal systems. Many Southeast Asian economies continue to rely heavily on indirect taxes, such as value-added tax (VAT), which are regressive in nature. A shift toward more progressive income and property taxation, alongside measures to curb tax evasion and avoidance, is necessary to fund redistributive spending without exacerbating burdens on the poor (Bahl & Bird, 2008; Asian Development Bank, 2021). The challenge, however, lies in overcoming resistance from entrenched interests and ensuring that tax reforms are not only technically sound but also politically feasible (IMF, 2021).

The heterogeneity observed across countries underscores the need for context-specific policy design. While some fiscal instruments may be universally beneficial, such as investments in basic education and primary healthcare, others need to be calibrated to the socio-political and institutional environment (World Bank, 2023). For example, conditional cash transfers (CCTs) may work effectively in countries with strong administrative oversight but may falter in fragile settings. Therefore, borrowing best practices must be accompanied by robust diagnostics and adaptive implementation strategies (Atkinson, 2015).

Institutionalization of accountability mechanisms also emerges as a key recommendation from this analysis. Transparent budgeting processes, citizen participation in monitoring public expenditure, and independent audit institutions can significantly enhance the efficiency and equity of fiscal interventions. This is supported by the Asian Development Bank (2021), which found that countries with stronger public financial management systems tend to exhibit better redistributive performance. Furthermore, integrating fiscal policy with broader social policy frameworks such as social protection floors and universal basic services can provide a more coherent and sustainable approach to addressing inequality (Jha, 2006; UNDP, 2020).

This study contributes to the growing body of literature emphasizing that redistribution is not merely a technical challenge but a political and institutional one. The commitment to equity must be embedded in national development strategies and supported by durable coalitions that advocate for inclusive fiscal reform. As highlighted by the UNDP (2020), human development is fundamentally about expanding people's choices and capabilities, which requires equitable access to resources and opportunities facilitated through fiscal policy.

While the potential of fiscal policy to reduce income inequality is well established, its effectiveness is contingent upon a combination of adequate fiscal resources, efficient administrative structures, and sustained political will. Southeast Asian countries offer a diverse set of experiences that provide valuable lessons. Moving forward, policymakers must prioritize progressive tax reforms, strengthen institutional frameworks, and design inclusive expenditure programs that are resilient to political and economic shocks. Only through such comprehensive and context-aware strategies can the promise of fiscal policy as a tool for social justice be fully realized.

CONCLUSION

This study underscores the significant yet uneven role of fiscal policy in reducing income inequality across Southeast Asian countries. The empirical findings affirm the theoretical propositions of redistributive fiscal policy, where government interventions through public spending and taxation can mitigate market-driven disparities. Countries with higher fiscal capacity, such as Vietnam and Thailand, demonstrate more effective redistribution outcomes, particularly through sustained investments in health and education. The role of administrative efficiency cannot be overstated. Countries that can accurately identify and reach intended beneficiaries, while minimizing leakages and corruption, tend to amplify the impact of their redistributive programs. Political commitment further shapes the long-term trajectory of fiscal equity. Thailand's policy consistency in social protection exemplifies how inclusive growth is achievable through durable political will, while Malaysia and Indonesia show more mixed results due to variability in policy execution and elite capture. The diversity among these five Southeast Asian economies highlights the need for context-specific fiscal strategies. A uniform policy prescription is unlikely to yield optimal outcomes across the region. Therefore, policymakers must pursue progressive tax reforms, strengthen public financial management systems, and institutionalize transparency and accountability in social spending. While fiscal policy remains a vital instrument for addressing inequality, its effectiveness hinges on a triad of factors: adequate fiscal space, efficient administration, and political resolve. Southeast Asian countries must commit to long-term, inclusive fiscal frameworks that prioritize equity without undermining macroeconomic stability.

Only then can fiscal policy evolve from a theoretical ideal into a practical solution for achieving just and inclusive development.

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