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Schooling and Labor Market Consequences of School
Construction in Indonesia: Evidence from an Unusual Policy
Experiment

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Abstract

Between 1973 and 1978, the Indonesian Government constructed over 61,000 primary schools throughout the country. This is one of the largest school construction programs on record. I evaluate the effect of this program on education and wages by combining differences across regions in the number of schools constructed with differences across cohorts induced by the timing of the program. The estimates suggest that the construction of primary schools led to an increase in education and earnings. Children aged 2 to 6 in 1974 received 0.12 to 0.19 more years of education for each school constructed per 1,000 children in their region of birth. Using the variation in schooling generated by this policy as instrumental variables for the impact of education on wages generates estimates of economic returns to education ranging from 6.5 percent to 10.6 percent. (JEL I2, J31, O15, O22)

The question of whether investment in infrastructure increases human capital and reduces poverty has long been a concern to development economists and policymakers. For example, availability of schooling infrastructure has been shown to be positively correlated with completed schooling or enrollment by Nancy Birdsall (1985) in urban Brazil, Dennis DeTay (1988) and Lee A. Lillard and Robert J. Willis (1994) in Malaysia, Victor Levy (1996) in Ghana, and Anne Case and Angus Deaton (1996) in South Africa. The principal methodological problem with these studies is that schools are not randomly allocated across communities. In education systems relying on local financing, more affluent communities can afford to build more schools. Children in these communities are likely to be more educated and earn more as adults. Alternatively, in centralized education systems, government resources may be allocated to regions that are lagging behind (as was the case with school construction in Indonesia in the 1970's). As a

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in their region of birth. Using the variations in schooling generated by this policy as instrumental variables for the impact of education on wages generates estimates of economic returns to education ranging from 6.8 percent to 10.6 percent.

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