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GOVERNANCE AND DEVELOPING ASIA: CONCEPTS, MEASUREMENTS, DETERMINANTS, AND PARADOXES

M. G. Quibria

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Governance and Developing Asia: Concepts, Measurements, Determinants, and Paradoxes

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ABSTRACT

Recent years have seen the emergence of a considerable volume of literature on governance and its role in economic and social development of a country. This paper provides a critical review of the literature. This review brings into the open a number of serious conceptual, measurement, and data issues as well as the existence of an Asian governance paradox—i.e., a general disjunction between growth and governance in most Asian economies. This paradox seems to suggest that much of the current policy discussion on governance is essentially faith-based. It calls into question the quality of the existing data and the analytical basis of the policy orthodoxy.

Keywords: government quality, corruption, bureaucracy, social capital

JEL Classification: O40, O43, P30, P48

I. INTRODUCTION

There is a broad consensus in the development community that governance has a critical bearing on economic and social outcomes. The international development agenda has reflected this prominently. In addition to being incorporated in the Millennium Development Goals (Goal 8 affirms “a commitment to good governance—both nationally and internationally”), governance is a critical determining criterion in the allocation of aid under the Millennium Challenge Account of the Government of the United States (US) and the International Development Association (IDA) resources¹ of the World Bank.² Following the lead of the World Bank, all multilateral development and financial institutions pursue an active agenda of governance reform in developing countries.

This agenda reflects the current development paradigm that views good governance as an essential ingredient of economic growth: Good governance has been suggested to lead to a more efficient division of labor, higher productivity of investment, and efficient implementation of social and economic policies (United Nations 2005). Economic growth aside, good governance is considered vital to ensuring favorable social and development outcomes by alleviating poverty, eliminating illiteracy, and reducing infant and maternal mortality. It has also been suggested that much of the development debacle of sub-Saharan Africa is due to its putative governance failures. Conversely, the spectacular economic achievements of most of developing Asia—which are associated with rapid economic transformation, poverty reduction, and concomitant improvements in social indicators—are inevitably attributed to the region’s success in ensuring good governance.

While such generalizations are intuitively appealing, they appear to fly in the face of facts. Many high-performing Asian economies do not by any means represent outstanding exemplars of good governance, at least by the metric of traditional measures of governance. It appears that a good deal of the current policy discussions on governance is not based on a systematic review of the empirical evidence.

This paper provides a critical review of the recent economic literature on governance. This review is, of necessity, selective, focusing on some salient aspects of governance. It begins in sections II–IV with discussions of concepts, measurements, and data issues. This examination brings into the open a number of serious conceptual, measurement, and data issues. It then moves on to an analysis of the determinants of governance in section V. Finally, the paper reviews the empirical relationship between growth and governance in the context of developing Asia. The review suggests the existence of an Asian governance paradox—i.e., a general disjunction between growth and governance in most Asian economies. This paradox seems to call into question the quality of the existing data as well as the analytical basis of much of the policy orthodoxy. The paper concludes with a brief sketch of an agenda for future reform in developing Asia.

¹ The IDA is a World Bank affiliate that provides assistance to the world’s 82 poorest countries. This assistance is in the form of interest-free loans and grants for programs for promoting economic growth and improving living conditions.

² Other multilateral development banks, including the Asian Development Bank (ADB), follow an aid allocation formula similar to the IDA.

II. WHAT DOES GOVERNANCE MEAN?

According to the American Heritage Dictionary (2011), governance is “the act, process or power of governing: principles of good governance.” This simple definition obscures the fact that governance is a complex concept with many different dimensions. Indeed, various authors have used the term governance in different senses, highlighting diverse aspects of governance (see Box 1). While some have used governance expansively to refer to the entire gamut of social, political, and legal institutions that have a bearing on the functioning of the government, others have used it to refer specifically to state capacity; and still others have used it as a code word for corruption and malfeasance of the government.

Box 1: Three Different Perspectives on Governance

Kaufmann and his collaborators in the World Bank website on Worldwide Governance Indicators provide the most expansive definition of governance. According to Kaufmann et al. 2013:

Governance includes the process by which governments are selected, monitored and replaced; the capacity of the government to effectively formulate and implement sound policies; and the respect of citizens and the state for the institutions that govern economic and social interactions among them.

This definition includes all the three dimensions discussed earlier: political regime, state capacity, and legal framework.

Princeton economist Avinash Dixit (2009), whose focus is the institutions of economic governance, defines governance in the following ways:

By economic governance I mean the structure and functioning of the legal and social institutions that support economic activity and economic transactions by protecting property rights, enforcing contracts, and taking collective action to provide physical and organizational infrastructure.

This definition is limited essentially to the structure and functioning of the legal institutions required for a smooth working of the market economy. This definition eschews the related issues of the nature of the political regime in which the market economy is embedded or the state capacity for economic management to ensure efficiency of the market system.

Stanford political scientist Francis Fukuyama (2013, p3), who is more concerned with the government’s economic management capacity, defines governance as “a government’s ability to make and enforce rules, and to deliver services, regardless of whether that government is democratic or not.”

In this definition, the nature of the political regime is not significant because, as Fukuyama (2013, p4) argues, governance is about performance or execution by the bureaucracy as opposed to politics or public policy: “An authoritarian regime can be well governed, just as a democracy can be mal-administered.” The efficiency of the bureaucracy to achieve its assigned objectives, according to Fukuyama, is determined by its capacity and autonomy. This interpretation is more concerned with the issue of state capacity and less with the issues of political regime or with the existence of an efficient legal structure in support of the market system, which is assumed implicitly.

In short, as should be obvious from the above brief discussion, governance remains a broad, multidimensional concept that lacks operational precision. It has often been used as an umbrella concept to federate an assortment of different, albeit related ideas.

Sources: Kaufmann et al. (2013); Dixit (2009); and Fukuyama (2013).

First, some have underscored *political regime*, relating to political contestability and election processes, political and civil liberties, and the legitimacy of the government. From this perspective, democracy, human rights, political rights, and freedom of the press are critical elements of good governance. In an environment of good governance, all policy decisions should be the outcome of a transparent, participatory, and accountable decision-making process.

Second, some have emphasized *state capacity* for economic management. This definition focuses on the soundness with which the government exercises its authority in the management of a country's social and economic resources. From this perspective, the quality of governance is reflected in the capacity of the government to design, formulate, and implement appropriate policies. It further assumes that sound economic management requires the support of an efficient bureaucracy, which is both capable and autonomous. Good governance, thus conceived, results in the adoption and implementation of appropriate policies, in improvement in the provision of public services, and in efficacious economic management that helps avoid delays of execution, malfeasance, and corruption.

However, designing an appropriate set of policies that can address the country's development problems successfully is much easier said than done. Appropriate policies depend not only on the specific objective of development—whether economic growth, poverty reduction, or lower inequality—but also on the social, political, cultural, and historical contexts. The classical view amongst economists, famously articulated by Smith (1776), has been that a good government protects property rights and keeps regulations and taxes light. In other words, a good government is relatively non-interventionist. However, this “minimalist view” of government no longer holds wide sway; a heterodox view that assigns a more expansive role for the government has replaced it. Nevertheless, in the 1990s, the Washington-based international financial institutions advocated a set of neoliberal policies, widely known as the Washington consensus (Williamson 1990). However, these policies became the subject of wide-ranging debates in the development community.³

Finally, some have focused on regulation of economic activities—particularly, the *legal frameworks*—which define, regulate, and mediate the interactions between the government and citizens, including the private sector and civil society. This definition highlights the separation, independence, and effectiveness of the judiciary, enforcement of contracts, securing property rights, and the rule of law. The latter means the supremacy of law, which applies equally without discrimination to all individuals and the government.

International financial institutions (IFIs), which are precluded by their charters from making forays into the political arena (though this prohibition has not deterred the leaderships of these

³ The Washington consensus policies proved sterile in rekindling growth. Despite the widespread application of these policies through structural adjustment programs in the 1980s and 1990s, growth rates in the developing world collapsed, compared with the 1960s and 1970s when these countries emphasized state interventions and import substitutions. As the failure of the Washington consensus became apparent, these policies were supplemented by additional policies: what has come to be known as the Washington consensus plus. The new policy agenda of the Washington consensus plus, however, was much more ad hoc and often hastily cobbled together. In the words of Stiglitz (undated), a former chief economist of the World Bank:

What was added (to the agenda) depended on the criticism that was being leveled, on the nature of the failure that was being recognized. When growth failed to materialize, ‘second generation reforms’, including competition policies to accompany privatizations of natural monopolies, were added. When problems of equity were noted, the plus included female education or improved safety nets. When all of these versions of the Washington consensus plus too failed to do the trick, a new layer of reforms was added: one had to go beyond projects and policies to institutions, including public institutions, and their governance.

organizations to occasionally deviate), have adopted a narrower, economic–technocratic approach to governance. This approach is concerned more with economic policies and effectiveness of state for sound economic management than with the broader societal issues such as the equity of the system or the legitimacy of the power structure. Consequently, the multilateral institutions have generally eschewed such political issues as democratization and human rights.

The World Bank defines governance as “the manner in which power is exercised in the management of a country’s economic and social resources for development” (World Bank, 1992, p.1). In more concrete terms, the World Bank’s primary concern in governance relates to sound development management—i.e., public sector reform, public expenditure control, fiduciary management, modernization of public administration, and privatization. In recent years, the World Bank governance policy appears to have gone through a shift, more toward anticorruption⁴ vis-à-vis other dimensions of governance (see World Bank 2007).

On the other hand, the International Monetary Fund’s (IMF) involvement in good governance has been limited to macroeconomic management. According to the IMF (1997), its governance agenda is “primarily concerned with macroeconomic stability, external viability, and orderly economic growth in member countries.” More specifically, the IMF focuses on two principal areas of governance: improving the management of public resources through reforms covering public sector institutions, and supporting the development and maintenance of a transparent and stable economic and regulatory environment conducive to efficient private sector activities.

Finally, ADB, the first multilateral development bank to adopt a formal governance policy in 1995, like the World Bank, defines governance as “sound development management.” However, the ADB definition is focused essentially on the “ingredients of effective management [of public resources].” While ADB recognizes the importance of good policies, it acknowledges, in light of “the experiences so far, especially within the region,” the existence of a plurality of views on good policies and on political systems (ADB 1995). In recent years, like the World Bank, anticorruption has occupied a large part of its governance agenda.

III. ALTERNATIVE INDICATORS OF GOVERNANCE

A. Taxonomy of Governance Indicators and Sources

If defining governance is a challenge, measuring it is even harder. Despite this challenge, recent years have seen the emergence of an active enterprise devoted to the task of producing indicators of governance. Production of indicators of governance and institutions is now the preoccupation of many organizations and individuals. However, these governance indices are quite heterogeneous. They tend to differ in terms of quality and coverage—geographical as well as temporal.

⁴ The rhetoric of corruption reached a crescendo during the shortened tenure of the World Bank President Wolfowitz (2006), who declared:

Today one of the biggest threats to development in many countries is corruption. It weakens fundamental systems, it distorts markets, and it encourages people to apply their skills and energies in nonproductive ways. In the end, governments and citizens will pay a price, a price in lower incomes, in lower investment, and in more volatile economic fluctuations. ... Corruption not only undermines the ability of governments to function properly, it also stifles the growth of the private sector.

Governance indicators can be divided into two broad types. Some are facts-based, grounded on objective macroeconomic economic data; and some are opinion-based, derived from subjective interpretations of experts of laws and constitutions or the experiences of citizens or businesses. Governance indicators can also be divided between de facto and de jure indicators. For example, data used to construct facts-based indicators often capture only formal de jure realities; they do not reflect de facto realities, which are often determined by informal and unwritten conventions and practices and shape the true quality of governance in a country. Thus, for example, the existence of strict anticorruption laws or an anticorruption bureau does not necessarily imply lower de facto corruption in one country compared with another that does not have those laws or a bureau; the formal creation of an anticorruption bureau may not reflect the seriousness with which a country actually prosecutes corruption. Similarly, a larger number of legal prosecutions for acts of corruption in one country compared with another does not imply a lower level of corruption in the first country compared with the second.

An important feature of facts-based indicators vis-à-vis perception-based indicators should be noted: facts-based indicators are replicable and hence more transparent than perception-based indicators. However, this does not imply that the facts-based governance indicators are necessarily more objective; even facts-based indicators embody a significant degree of subjective judgment—in the choice of facts as well as in the interpretation (how variations in those facts tend to affect the quality of governance).

Table 1: Governance Indicators: Sources and Types of Information

Source of information	Type of indicator			
	Facts-based/De Jure		Perception-based/De Facto	
	Broad	Specific	Broad	Specific
<i>Experts</i>				
Lawyers and accountants		DB		
Commercial risk-rating agencies			DRI, EIU, PRS	
Nongovernment organizations		GII	HER, RSF, CIR, FRH	GII, OBI
Governments and multilaterals			CPIA	PEFA
Academics	DPI, PIV		DPI, PIV	
<i>Survey respondents</i>				
Firms				ICA, GCS, WCY
Individuals			AFR, LBO, GWP	
<i>Aggregate indicators combining experts and survey respondents</i>			WGI, MOI	TI

AFR = Afrobarometer, CIR = Cingranelli-Richards Human Rights Dataset, CPIA = Country Policy and Institutional Assessment, DB = Doing Business, DPI = Database of Political Institutions, DRI = Global Insight DRI, EIU = Economist Intelligence Unit, FRH = Freedom House, GCS = Global Competitiveness Survey, GII = Global Integrity Index, GWP = Gallup World Poll, HER = Heritage Foundation, ICA = Investment Climate Assessment, LBO = Latinobarometro, MOI = Ibrahim Index of African Governance, OBI = Open Budget Index, PEFA = Public Expenditure and Financial Accountability, PIV = Polity IV, PRS = Political Risk Services, RSF = Reporters Without Borders, TI = Transparency International, WCY = World Competitiveness Yearbook, WGI = Worldwide Governance Indicators.

Source: Adapted from Kaufmann and Kraay (2008).

There are many more perception-based indicators than facts-based indicators. There are two reasons for this. First, the data required to construct facts-based indicators are often not available for developing countries (or the information that exists for those countries may lack credibility). Second, there may be a greater demand for perception-based indicators from the business investors for

commercial purposes. The data used to construct facts-based indicators refer to formal de jure realities, which do not reflect de facto realities—facts on the ground, which are often determined by informal and unwritten rules and practices.

Table 1, adapted from Kaufmann and Kraay (2008), provides a quick guide to the major governance indicators with regard to their sources and types of information used.

B. Review of Some Selective Indicators⁵

1. World Economic Forum

Global Competitiveness Index: The World Economic Forum has published a yearly Global Competitiveness Report since 1979. This report ranks countries based on the Global Competitiveness Index (GCI). The GCI attempts to codify the impact of a number of key factors—such as the macroeconomic environment, the quality of the country’s institutions, and the state of the country’s technology and supporting infrastructure—into a single index of competitiveness.

The latest *Global Competitiveness Report 2012–2013* ranks the competitiveness of 144 economies. The ranking is based on more than 110 variables, two-thirds of which come from the Executive Opinion Survey from a sample of business leaders in their respective countries. The number of respondents for the Executive Opinion Survey has increased over the years, currently exceeding the total of 14,000 in 144 countries. The remaining one-third of the data is obtained from publicly available data sources, including international organizations, such as the United Nations and the IMF. The variables are organized into 12 pillars, with each pillar representing an important determinant of competitiveness. The report assumes that the impact of each pillar on competitiveness varies across countries, depending on their stages of economic development. Accordingly, GCI attaches different weights to different pillars depending on the income of the country. The weights are the values that best explain growth in recent years. For example, the sophistication and innovation factors contribute 10% to the final score in the factor- and efficiency-driven economies, but 30% in the innovation-driven economies (intermediate values are used for economies in transition between stages, see Table 2).

Table 2: Subindex Weights and Income Threshold for Stages of Development

	STAGES OF DEVELOPMENT				
	Stage 1: Factor-driven	Transition from stage 1 to stage 2	Stage 2: Efficiency- driven	Transition from stage 2 to stage 3	Stage 3: Innovation- driven
GDP per capita (\$) thresholds*	<2,000	2,000–2,999	3,000–8,999	9,000–17,000	>17,000
Weight for basic requirements subindex	60%	40%–60%	40%	20%–40%	20%
Weight for efficiency enhancers subindex	35%	3%–50%	50%	50%	50%
Weight for innovation and sophistication factors	5%	5%–10%	10%	10%–30%	30%

GDP = gross domestic product.

Notes: See individual country/economy profiles for the exact applied weights.

* For economies with a high dependency on mineral resources, GDP per capita is not the sole criterion for the determination of the stage of development. See text for details.

Source: World Economic Forum (2012).

⁵ This subsection is based mostly on information drawn from the websites of various governance indicators discussed.

2. Transparency International

Corruption Perceptions Index: Since 1995, Transparency International has published a Corruption Perceptions Index (CPI). The CPI annually ranks countries according to the extent to which corruption is believed to exist, as determined by expert assessments and opinion surveys. The CPI views corruption as the abuse of public power for private benefit. Since 2012, the CPI has ranked 176 countries on a scale of 100 (very clean) to 0 (highly corrupt). (In years prior, the scale ran from 10 to 0.) The 2012 CPI draws on 13 different surveys and assessments from 12 different institutions. The 13 surveys/assessments are either opinion surveys of businesspeople or performance assessments from risk-rating agencies and international organizations.

Bribe Payers Index: Transparency International has published a Bribe Payers Index (BPI) since 1999. The BPI, which is issued every 2–3 years, focuses on the supply side of corruption—it measures the willingness of a nation to comply with demands for corrupt business practices.

The BPI 2011 ranked 22 leading exporting countries, whose combined exports represented 80% of the world total in 2011, on the likelihood of their multinational businesses to use bribes while operating abroad. The ranking is based on the responses by business executives, as captured in the Bribe Payers Survey. Countries are scored on a scale of 0 to 10, where the higher scores suggest a lower likelihood of using bribery (the lowest score 1 indicates a country situation where bribes are common or even mandatory and the highest score 10 a situation where companies from that country never bribe abroad).

3. Heritage Foundation

Index of Economic Freedom: Since 1995, the Heritage Foundation, in conjunction with *The Wall Street Journal*, has published an annual Index of Economic Freedom, which ranks nations according to the degree of economic freedom.⁶ The index, which now covers 162 countries, is based on 10 individual freedoms: business freedom, trade freedom, fiscal freedom, government size, monetary freedom, investment freedom, financial freedom, property rights, freedom from corruption, and labor freedom. These 10 economic freedoms are aggregated, with an equal weight assigned to each freedom, to derive an overall freedom index. In deriving the overall score, each individual freedom is graded on a scale of 0 to 100, where the maximum freedom is represented by 100 (a score of 100 indicates an economic environment—or a set of policies—most conducive to economic freedom). The methodology is revised as new data and measurements become available. In 2007, a new indicator of freedom, called labor freedom, was added to reflect workers' rights to work—as much and wherever. The entire series is revised for consistency each time changes in methodology are introduced.

4. World Bank

Country Policy and Institutional Assessment: Produced annually by World Bank staff since the mid-1970s, the Country Policy and Institutional Assessment (CPIA) provides an annual review of the quality of policy and institutional performance in 136 borrowing countries. While earlier assessments focused mainly on macroeconomic policies, they now include such areas as social inclusion, equity, and governance. The CPIA rates countries against a set of 16 criteria, which are grouped in four

⁶ Economic freedom—which is defined as the condition in which individuals can act with maximum autonomy in the pursuit of their livelihood and economic prosperity—is grouped into four major types of freedom: (i) rule of law; (ii) limited government; (iii) regulatory efficiency; and (iv) open markets.

clusters: (i) economic management; (ii) structural policies; (iii) policies for social inclusion and equity; and (iv) public sector management and institutions, including “Transparency, Accountability, and Corruption in the Public Sector.” For each of the 16 criteria, countries are rated on a scale of 1 (low) to 6 (high). The scores depend on the level of performance in a given year, which is assessed against the criteria, rather than on changes in performance compared with the previous year. The ratings depend on actual policies and performance, rather than on promises or intentions. In some cases, measures such as the passage of specific legislation can represent an important action (though in the end, the *implementation* of legislation determines the extent of its impact). The ratings are the product of staff judgment. The World Bank’s IDA Resource Allocation Index (IRAI) is based on the results of the annual CPIA exercise. Since 2005, CPIA ratings have been disclosed partially to the public.

The World Bank has reexamined the CPIA criteria periodically and revised them to reflect both the lessons of experience and its evolution in thinking about development. Over time, the assessment criteria have evolved: they now include not only macroeconomic indicators—as it was the case earlier—but also governance and other social and structural indicators. Notwithstanding these improvements, the CPIA continues to be highly contentious. As Streets (2008) notes, some common criticisms include: the CPIA essentially reflects the Washington consensus; it is prescriptive in its underlying assumptions about the character of good policies and institutions; it is historic and blind to country-specific characteristics; and the CPIA rating process lacks internal consistency and is not sufficiently robust.

Doing Business Index: The World Bank’s project on Doing Business gathers and analyzes data to compare the business regulatory environment across economies and over time. The project seeks to capture the ease of doing business by assessing formal regulations and procedures that impact domestic small and medium-sized enterprises.

The first report, which was published in 2003, included 133 economies and covered five indicator sets. The report updates all these indicators on a yearly basis and constructs an Ease of Doing Business Index to rank countries. This aggregate index, which currently covers 10 indicators, is a simple average of the percentile rankings on each of the indicators. The 10 different indicators include the number of procedures, time, and costs required for complying with formal requirements in 10 regulatory areas: (i) starting a business; (ii) dealing with construction permits; (iii) getting electricity; (iv) registering property; (v) getting credit; (vi) protecting investors; (vii) paying taxes; (viii) trading across borders; (ix) ensuring contracts; and (x) resolving insolvency. Prior to 2013, the report also included an indicator on employing workers—which measures the ease with which workers can be hired and fired and the rigidity of working hours—in determining the aggregate ranking of countries. However, this labor indicator—which is perhaps consistent with the letter, but not with the spirit of ILO regulations—has proved controversial. Currently, in the face of continuing criticism, the Doing Business project only gathers and publishes information on employing workers but does not use it in the Ease of Doing Business Index.

For its index, the Doing Business project uses a hypothetical “standard” firm, which is a privately held, domestically owned, limited liability company with 10–50 employees operating in the country’s largest business city. It explicitly assumes full compliance with regulation, the existence of no third parties to facilitate completing procedures, and no bribe payments or other activities to influence policy outcomes. One to four lawyers or accountants in each country compile the data; they base their assessments of the typical time and cost of complying with the regulations, based on actual wording of the regulations as they exist on the books. These Doing Business indicators purport to measure the

business friendliness of a country's regulatory environment. A higher ranking indicates a more business-friendly environment with fewer and simpler regulations for businesses.

Worldwide Governance Indicators: Of all the global indicators of governance, those from the World Bank's Worldwide Governance Indicators (WGI) appear to have emerged as the industry leader. They are the most comprehensive and the most influential. Besides its popularity among many social scientists, the Millennium Challenge Corporation of the US government uses this dataset for its aid allocation purposes.

The WGI dataset covers more than 200 countries over the period 1996–2011 and presents information on six aggregate indicators: voice and accountability; government effectiveness; political stability and absence of violence; regulatory quality; rule of law; and control of corruption. Voice and accountability considers various aspects of the political process, civil liberties, and political rights. Government effectiveness incorporates measures on the quality of public service provision, the quality of bureaucracy, the insulation of the civil service from political pressures, and the credibility of the government commitment to policies. Regulatory quality measures the incidence of market-friendly policies and the burdens from excessive regulations. Rule of law includes indicators that gauge the confidence of the agents in—and their compliance with—the rules of society. The final set of indicators measures the perception of corruption in the government.

The WGI dataset, which is an amalgam of governance data from a wide variety of sources—polls of experts and surveys of businesspeople and general citizens. The governance estimate for each aggregate indicator is derived from individual sources in each period and is normalized so that it has a mean of 0 and standard deviation of 1. This means that virtually all the scores lie between –2.5 and 2.5, and the aggregate indicators are measures of relative performance of a country in a particular period (the higher the score of a country, the better is its performance in terms of governance).

The WGI compile and summarize information from 30 existing data sources (see Table 3). These data sources can be grouped into four different types: (i) Surveys of households and firms (nine data sources, including the Afrobarometer surveys, Gallup World Poll, and Global Competitiveness Report survey); (ii) commercial business information providers (four data sources, including the Economist Intelligence Unit, Global Insight, and Political Risk Services); (iii) nongovernment organizations (nine data sources, including Global Integrity, Freedom House, and Reporters Without Borders); and (iv) public sector organizations (eight data sources, including the CPIA assessments of the World Bank and regional development banks, the EBRD Transition Report, and French Ministry of Finance Institutional Profiles Database).

Table 3: Data Sources for WGI: 2012

Code	Source	Type*	Public	Country Coverage	Representative	1996	1998	2000	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
ADB	African Development Bank Country Policy and Institutional Assessments	Expert (GOV)	Partial	54		x		x	x	x	x	x	x	x	x	x	x	x
AFR	Afrobarometer	Survey	Yes	20					x	x	x	x	x	x	x	x	x	x
ASD	Asian Development Bank Country Policy and Institutional Assessments	Expert (GOV)	Partial	28				x	x	x	x	x	x	x	x	x	x	x
BPS	Business Enterprise Environment Survey	Survey	Yes	30				x	x	x	x	x	x	x	x	x	x	x
BTI	Bertelsmann Transformation Index	Expert (NGO)	Yes	128				x	x	x	x	x	x	x	x	x	x	x
CCR	Freedom House Countries at the Crossroads	Expert (NGO)	Yes	69						x	x	x	x	x	x	x	x	x
EBR	European Bank for Reconstruction and Development Transition Report	Expert (GOV)	Yes	29		x	x	x	x	x	x	x	x	x	x	x	x	x
EIU	Economist Intelligence Unit Riskwire & Democracy Index	Expert (CBIP)	Yes	180	x	x	x	x	x	x	x	x	x	x	x	x	x	x
FRH	Freedom House	Expert (NGO)	Yes	29	x	x	x	x	x	x	x	x	x	x	x	x	x	x
GCB	Transparency International Global Corruption Barometer Survey	Survey	Yes	89				x	x	x	x	x	x	x	x	x	x	x
GCS	World Economic Forum Global Competitiveness Report	Survey	Yes	136		x	x	x	x	x	x	x	x	x	x	x	x	x
GII	Global Integrity Index	Expert (NGO)	Yes	70						x	x	x	x	x	x	x	x	x
GWP	Gallup World Poll	Survey	Yes	147	x									x	x	x	x	x
HER	Heritage Foundation Index of Economic Freedom	Expert (NGO)	Yes	179	x	x	x	x	x	x	x	x	x	x	x	x	x	x
HUM	Cingranelli Richards Human Rights Database and Political Terror Scale	Expert (GOV)	Yes	194	x	x	x	x	x	x	x	x	x	x	x	x	x	x
IPD	IFAD Rural Sector Performance Assessments	Expert (GOV)	Yes	112						x	x	x	x	x	x	x	x	x
IJT	IJET Country Security Risk Ratings	Expert (CBIP)	Yes	190	x					x	x	x	x	x	x	x	x	x
IFD	Institutional Profiles Database	Expert (GOV)	Yes	123	x					x	x	x	x	x	x	x	x	x
IRP	IREEP African Electoral Index	Expert (NGO)	Yes	53				x	x	x	x	x	x	x	x	x	x	x
LBO	Latinobarometro	Survey	Yes	18		x	x	x	x	x	x	x	x	x	x	x	x	x
MSI	International Research and Exchanges Board Media Sustainability Index	Expert (NGO)	Yes	61						x	x	x	x	x	x	x	x	x
OBI	International Budget Project Open Budget Index	Expert (NGO)	Yes	93						x	x	x	x	x	x	x	x	x
PIA	World Bank Country Policy and Institutional Assessments	Expert (GOV)	Partial	136										x	x	x	x	x
PRC	Political Economic Risk Consultancy Corruption in Asia Survey	Survey	Yes	16		x	x	x	x	x	x	x	x	x	x	x	x	x
PRS	Political Risk Services International Country Risk Guide	Expert (CBIP)	Yes	140		x	x	x	x	x	x	x	x	x	x	x	x	x
RSF	Reporters Without Borders Press Freedom Index	Expert (NGO)	Yes	175	x					x	x	x	x	x	x	x	x	x
TPR	US State Department Trafficking in People Report	Expert (GOV)	Yes	184	x			x	x	x	x	x	x	x	x	x	x	x
VAB	Vanderbilt University Americas Barometer	Survey	Yes	25										x	x	x	x	x
WCY	Institute for Management and Development World Competitiveness Yearbook	Survey	Yes	59		x	x	x	x	x	x	x	x	x	x	x	x	x
WMO	Global Insight Business Conditions and Risk Indicators	Expert (CBIP)	Yes	203	x	x	x	x	x	x	x	x	x	x	x	x	x	x

*Types of expert assessments: CBIP = commercial business information provider, GOV = public sector data provider, NGO = nongovernment organization data provider.

Source: World Bank (2013).

IV. MEASUREMENT ISSUES

This section describes some of the salient measurement issues that relate to the aggregate governance indicators.

A. Validity, Reliability, and Precision

The performance of a governance indicator can be judged by three criteria: validity, reliability, and precision (Johnston 2008). Validity refers to whether or not the indicator actually measures what it intends to measure; in other words, the measures should be on target with small nonsystematic errors. Reliability refers to whether a repeated application of the measurement tool by a variety of users will return consistent results. Precision denotes small measurement errors in the governance indicator. The current body of governance indicators, whether facts-based or perception-based, seems to fall short of the ideal on all three counts.

All governance indicators are attempts at approximating some unobserved broad dimensions of governance. However, the process of approximating the unobserved dimensions is fraught with difficulties. To begin with, there is the complex problem of translating perceptions into quantities. This problem is further compounded by the fact that perceptions do not necessarily reflect objective reality: perceptions of governance are not the same as the actual state of governance. As Thomas (2010) has forcefully argued, there is a substantial difference between measuring something and measuring perceptions of it. Drawing on a number of empirical studies, she contends that perceptions of crime risk are quite different than actual crime levels; perceptions of corruption are different from actual corruption levels; and trust in government is different from administrative performance. This chasm between perceptions and reality stems from a number of sources. First, perceptions can lag behind reality in a dynamic economic context, when the structure and policies of an economy are undergoing rapid changes. Second, perceptions can be biased due to the “halo effect”: experts making similar errors when considering the same country. This correlation in the perception errors derives from the fact that experts rely on the same data sources or similar media reports in assessing an individual country. Finally, many of the governance indicators are based on the assessments of foreign respondents, whose perceptions can be biased for ideological and cultural reasons (as social norms vary across societies).

Similarly, facts-based governance indicators can be a poor reflection of the reality of governance in a developing country, because of the large gap between *de jure* rules and regulations and *de facto* realities (which are conditioned by informal rules, customs, and conventions). In this connection, one may note the stark contrast in results between the World Bank’s Doing Business and the Enterprise Surveys (Hallward-Driemeier and Pritchett 2011). These two surveys use different approaches to assessing the governance constraints facing the private sector. The Doing Business project provides measures of compliance with regulatory requirements and the Enterprise Surveys provide firms’ reported experiences with regulations and other investment climate conditions. Hallward-Driemeier and Pritchett (2011) note that for the 80 countries that have both Doing Business and ES results, the average days to obtain a construction permit in the Doing Business far exceed those of the ES—by almost three times (177 days against 64 days). In other words, Hallward-Driemeier and Pritchett (2011) found little or no relationship between *de jure* and *de facto* measures of regulations. In sum, reliability remains an enormous issue: it is difficult for anyone other than the producers of these indicators to replicate the results, as many of the underlying surveys are not available to outsiders. Thus, the problem of reliability compounds as the number of surveys increases.

Finally, all governance indicators are particularly vulnerable to various measurement errors as they are gathered from many different types of data—surveys of different sizes with dissimilar contents. Some of these surveys ask questions about the country while others about agencies; many of the surveys are seldom revised whereas many others are revised regularly from year to year. Some country indicators are based on one or two sources of information while others are based on many. Given this data heterogeneity, governance indicators tend to suffer from large measurement errors—especially those for low-income countries with fewer sources of information.

B. The Single Number Problem

The standard governance measures compress a large amount of complex information into a single number for a country for a given year. The underlying data can be quite heterogeneous and the weight accorded to a particular type of data can be arbitrary. Consider, for example, the indicators of corruption, which can come in many different forms: In some countries, corruption can be petty and pervasive, while in others it may involve a few but major cases, comprising large sums of money. Similarly, the major types of corruption in some countries can be bureaucratic, while in others it can be political. In some, corruption can simply take the form of extensive nepotism without explicit financial transactions. Different individuals can have different perceptions about different types of corruption and rank them differently. It has been suggested that, given the diversity of values and the heterogeneity of indicators, there is no index of corruption that can meaningfully capture all such complexities in a single number (Johnston 2008).

The single number problem is a generic issue with all “mashup” indices, which Ravallion (2010) defines as those composite indices for which existing theory and practice provide little or no guidance to their design.⁷ Ravallion includes in this category of indices the Human Development Index, the WGI, and the Doing Business Ease of Doing Business Index. The fundamental shortcomings of these indices—which are encapsulated in the single number problem—relate to their meaning, interpretation, and robustness.

C. Intertemporal Comparability

Although the existing aggregate indices provide governance data over time, they often do not afford meaningful intertemporal comparisons. There are a number of reasons for this, some of which are specific to a particular index. In the case of the WGI, there are two important reasons for this lack of comparability across time. First, data sources are not fixed: the number of surveys, as well as their contents, has changed with time. Even in the absence of any real variation in the quality of governance, this changing composition of data sources can have a perceptible impact on the indicator values and the rankings of countries across years.⁸ Second, each of the composite WGI is computed in such a way that the average value is always 0 and its standard deviation is 1. This technical feature of the WGI implies that the scale is largely arbitrary and cannot be used for measuring changes over time, either globally, or for individual countries, or between specific groups of countries (Arndt 2009).

⁷ Ravallion (2010) describes the mashup index as an index with an unusually large number of moving parts that the producer of the index is essentially free to set arbitrarily. Ravallion suggests that the popularity of these indices is largely due to their parsimony: they collapse multiple dimensions into just one, which yields unambiguous country rankings and at the same time reduces concerns about measurement errors in the component series.

⁸ Arndt (2009) provides some concrete examples of changes in the number and composition of data sources in the WGI over time, and discusses how they have had a significant impact on the ratings of countries.

Likewise, the CPI of Transparency International suffers from similar problems of intertemporal comparability. It, however, clearly warns its users that year-to-year changes in a country's score can result from either a change in the perception of a country's performance or a change in the CPI's sample and methodology.

Finally, the Doing Business index has its own share of problems with respect to intertemporal comparability. Country ranking can be highly volatile over time for reasons that do not correspond to the real changes in the cardinal values of the indicators. As noted in a recent evaluation report of the World Bank (2008), a slight change in data and methodology can wreak havoc with the rankings: for example, some minor data revisions in 2007 greatly changed the rank positions of Italy and Guyana by 33 and 40 positions, respectively.

Notwithstanding these weaknesses, governance rankings are popular among politicians and policy makers because of their simplicity and intuitive appeal. The rise and fall of a country's governance rankings in the CPI or Doing Business indices often invokes heated political discussions in developing countries. The various governance datasets have also been popular with empirical economists engaging in cross-country regression analyses. The challenge of serious data shortcomings has not deterred many economists from undertaking in all manner of statistical analyses, including correlating intertemporal changes in governance indicators with changing growth rates or other development indicators (Baland, Moene, and Robinson 2010).

D. Lack of Actionability

While the current crop of governance indicators may have been helpful in placing governance issues on the development agenda, they have generally lacked in policy orientation. Moreover, many of the indicators have little or no correlation with the broad measures of economic performance at the country level. Given the limited use of governance indicators for policy purposes, they have so far made little direct contribution to policy making.

To be useful for policy purposes, the indicators need to be “actionable.” Actionability of indicators requires sharp definitions and clear specificity, comprising a plan for concrete actions, a strategy of reform, and a metric for measuring impacts. However, the concept of an actionable indicator assumes that the results chains—i.e., the link between policy action and policy outcomes—are known with certainty. This is not necessarily the case in reality; in the absence of such perfect knowledge, it has been argued that actionable indicators may not always be “action worthy” (Kaufmann and Kraay 2008).

E. Final Observations

In addition to the above statistical and measurement issues, the current body of governance indicators has also been criticized on ideological and conceptual grounds. A case in point is the World Bank's WGI and Doing Business indicators. Although they may not be based on any explicit theory, they tend to favor minimum government or lower environmental and labor protection. For example, the WGI use the indicator “Environmental regulations hurt competitiveness” from the World Economic Forum's Executive Opinion Survey, but ignores several questions of the survey that give high ratings to countries with a high standard of environmental protection. Similarly, the Doing Business indicator provides higher ratings to countries with fewer regulations, ignoring safety and environmental concern.

As a consequence, it is often unclear whether a top position in the Doing Business rankings represents good and efficient regulations or simply inadequate regulations (World Bank 2008).⁹

V. DETERMINANTS OF GOVERNANCE INDICATORS

A considerable body of writing deals with the various influences that shape the state of governance in a society. Rather than venturing into a new, original empirical exercise, this section will review and synthesize the existing body of literature. In so doing, it will seek to sort out the role of various historical, geographical, political, social, and cultural factors in shaping the state of governance in a particular country.

A. History

The fundamental institutional architecture of governance of a country is enshrined in its legal system. However, this legal system, in almost all countries, is often a happenstance of history—rather than an outcome of a long evolutionary process.

There are two major strands of legal traditions in the world: common law and civil law. Within the civil law tradition, there are several subsystems: French, German, Socialist, and Scandinavian. While it is possible that a country adopts some laws from one system and other laws from another, ultimately a particular tradition dominates. An important fact about legal traditions is that they have been transplanted from a relatively few sources to the rest of the world, mostly through colonization. Such transplantation covers specific laws and codes, as well as the general styles and ideologies of the legal system.

The common law tradition comprises the laws of England and of the former colonies, including Canada, the US, India, and Singapore. Common law is largely precedent-based and generally uncodified: it does not rely on a comprehensive compilation of legal rules and statutes (legislative decisions). Originating in Roman law, the civil law tradition, on the other hand, is based on a comprehensive set of legal codes (encompassing substantive procedural and penal laws). In terms of style and ideology, while the common law tradition maintains a strict independence of the judiciary from other branches of the government, such separation is less pronounced in the civil law tradition. Aside from dissimilar legal rules, a fundamental difference between the two systems is that the civil law system is more compatible with the concept of a centralized and activist government.

Within the civil law tradition, the French system has wielded a great influence on the German system, and, despite their similarities, the Germany system affords a greater degree of judicial law-making than the French system. The German tradition has had a great influence on the legal systems of Asian countries, such as the People's Republic of China (PRC), Japan, the Republic of Korea, and Turkey—though none were ever a German colony. The Scandinavian legal system is somewhat unique in the civil law tradition: a hybrid of civil law (drawn from Germany and France) and Scandinavian customary law. Never colonial powers, this tradition has few followings outside Scandinavia.

⁹ To review the Doing Business report, the World Bank appointed a panel of external experts, which identified numerous weaknesses in the report, relating to data collection, methodology, and governance of the project. The panel recommended that the World Bank publish a much more streamlined report without the overall aggregate rankings of countries (Manuel et al. 2013).

B. Geography

A recent body of studies suggests that geography played an important role in the European colonization strategy and had a decisive influence in determining the foundation for institutions of governance that exist in many countries today.

According to Hall and Jones (1999), Western Europeans avoided the tropics and settled in areas with climates similar to Western Europe; wherever they permanently settled, they brought with them their high-quality institutions.

According to Acemoglu, Johnson, and Robinson (2001, 2002), European colonizers did not permanently settle in the geographical environments that caused high settler mortality; in high-mortality areas, colonizers settled in small numbers and established extractive economies and institutions, mainly to transfer resources from the colony to the mainland. The colonizers also avoided prosperous geographical areas with high population density and urbanization. They preferred places with low population density, a congenial hosting population, and less local resistance. In places colonizers settled in large numbers, they introduced European-style institutions with the rule of law, property rights, and some constraints on the power of the elites. Based on their settlement strategy, Europeans settled in North America, Australia, and New Zealand but did not settle in Congo, Burundi, the Ivory Coast, Ghana, Bolivia, Mexico, and Peru, among others. According to this view, the governance structures created by colonialists in response to the environment endured even with the end of colonialism, as changes have proved to be costly to anyone who attempted them.¹⁰

According to Sokoloff and Engerman (2000) and Engerman, Haber and Sokoloff (2000), factor endowments had an important bearing on institutional development. Land endowments of Latin America were favorable to commodities (such as sugar cane, rice, and minerals) that allow economies of scale, and make use of slave or local indigenous labor. In Latin America, favorable resource endowments led to plantation agriculture and mining and a concentration of power in the hands of the plantation and mining elites. In contrast, land endowments in North America were favorable to family farming, which spurred the growth of a large middle class and a wide distribution of power once the power structure was formed; the elite in Latin America created institutions that preserved their hegemony, by restricting voting rights, public land, and mineral rights, and limiting access to schooling. These elite groups ultimately were opposed to democracy.

In contrast, North America enjoyed a larger middle class (with less powerful elite) that created more open and egalitarian institutions featuring broader voting rights, equal protection before the law, wider distribution of public lands and mineral rights, lower entry barriers to businesses, and public schooling. Differences in institutions between Latin America and North America also contributed to the larger European immigration flows to North America than to Latin America. In short, Latin America experienced a “resource curse” where favorable resource endowments led to “wrong” institutions.

Sachs and Warner (1995) and Sala-i-Martin and Subramanian (2003) argue that a natural resource abundance—such as oil and gas in Nigeria and Saudi Arabia—has led to sluggish development in institutions in some societies.

¹⁰ This theory has been challenged on both factual and technical econometric grounds. In a recent web post, Sachs (2012) provides a lucid, nontechnical summary of this body of criticisms.

C. Stage of Development

One of the well-established empirical facts about governance is that there is a positive relationship between per capita income and governance, irrespective of the indicator chosen. Figure 1 shows the correlation between the various composite governance indicators of the WGI and gross domestic product (GDP) per capita. As seen from the slope of the fitted regression lines and the estimated R-squared coefficients, government effectiveness and the rule of law have the highest correlation with a coefficient of .51 and R-squared of .66, respectively, while voice and accountability has the lowest correlation with per capita GDP with a coefficient of .39 and R-squared of .36. A composite index of governance (based on an average of all the six indicators) has a correlation with a coefficient of .47 and R-squared of .65. Altogether this seems to confirm a robust correlation between poor countries and poor governance. It also seems to highlight the fact that good governance requires abundant resources.

Figure 1: Governance Indicators and Per Capita Income

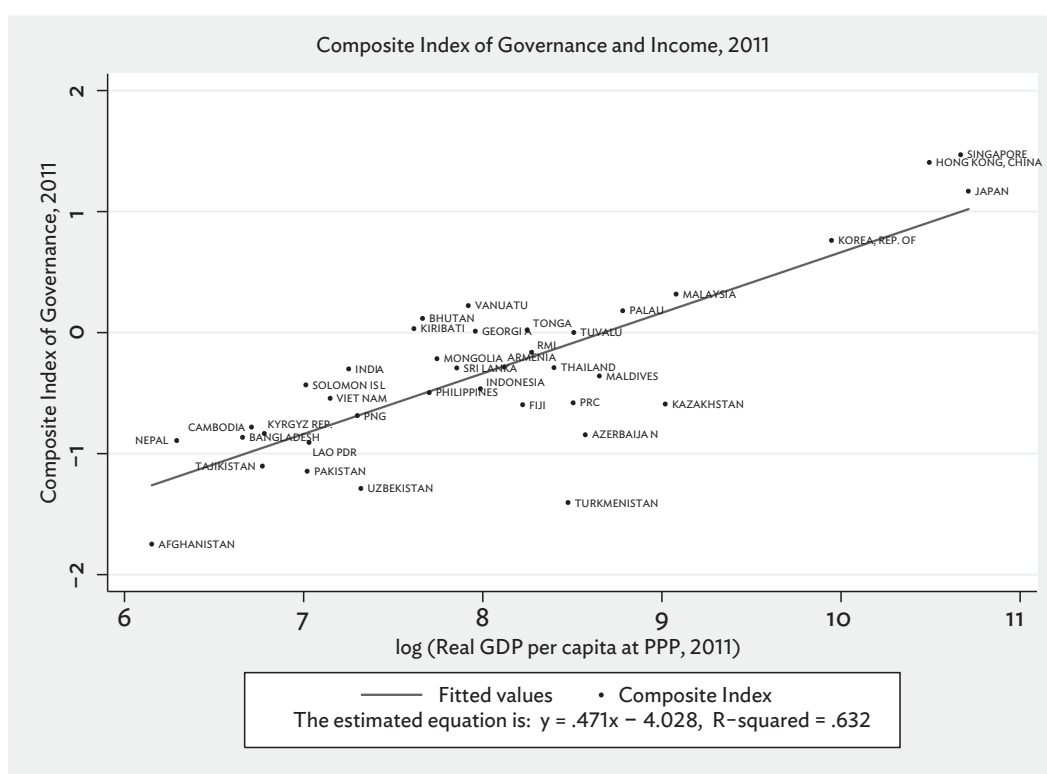


Figure 1: (continued)

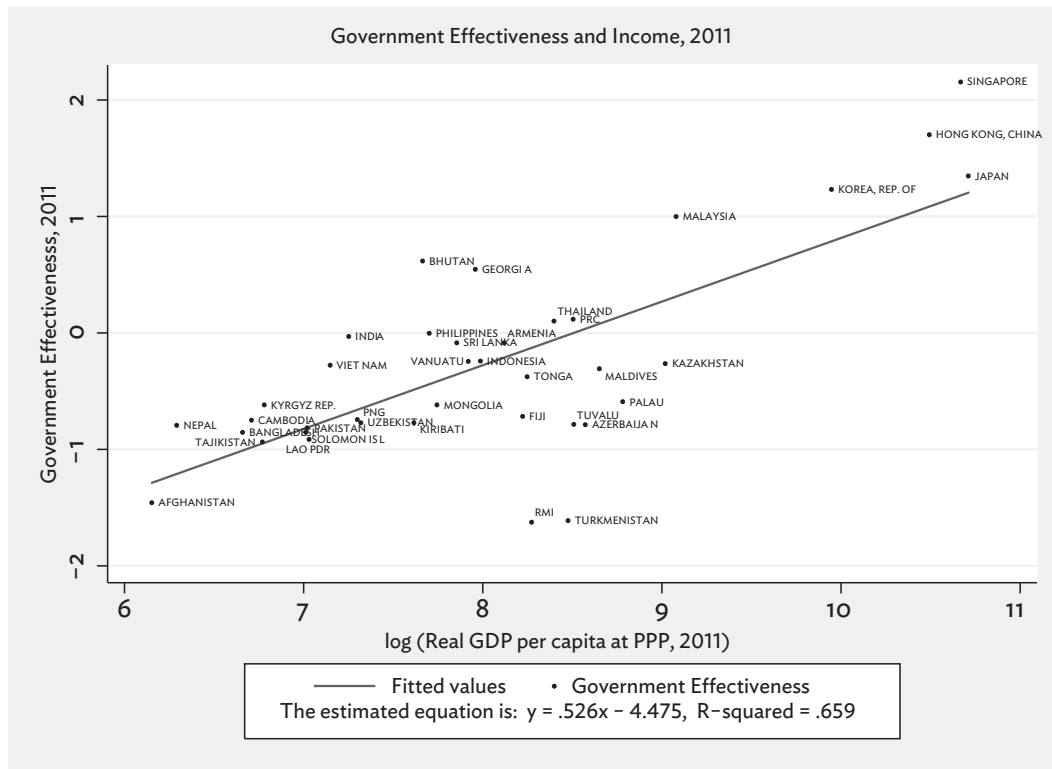
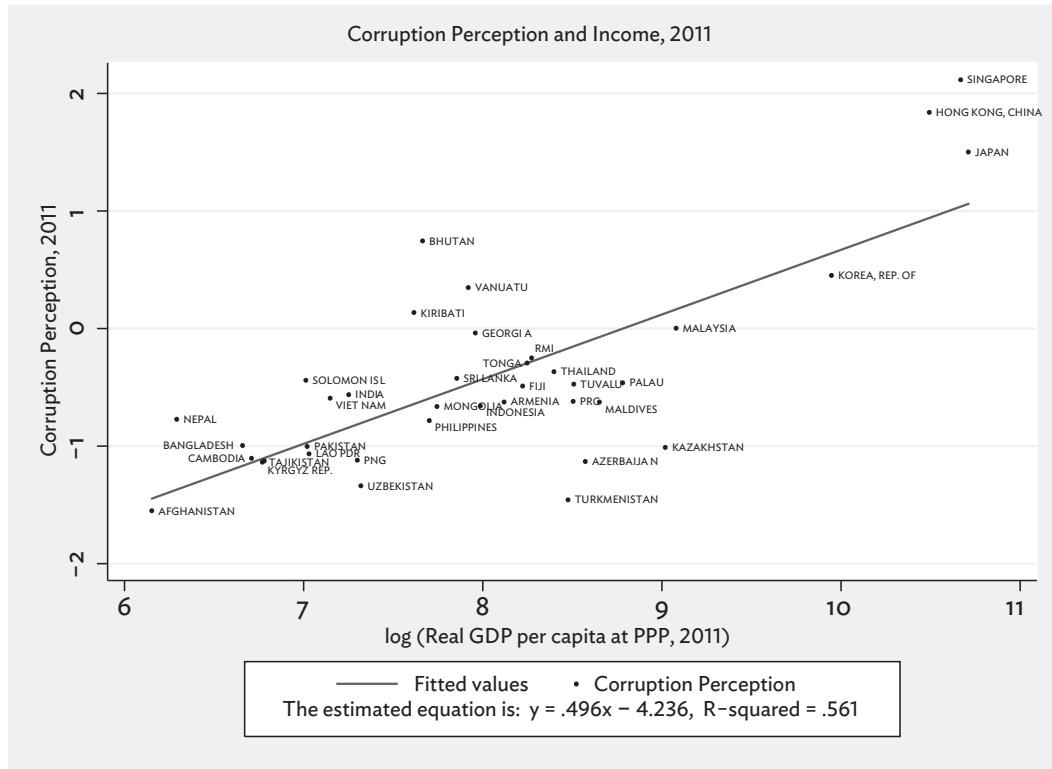


Figure 1: (continued)

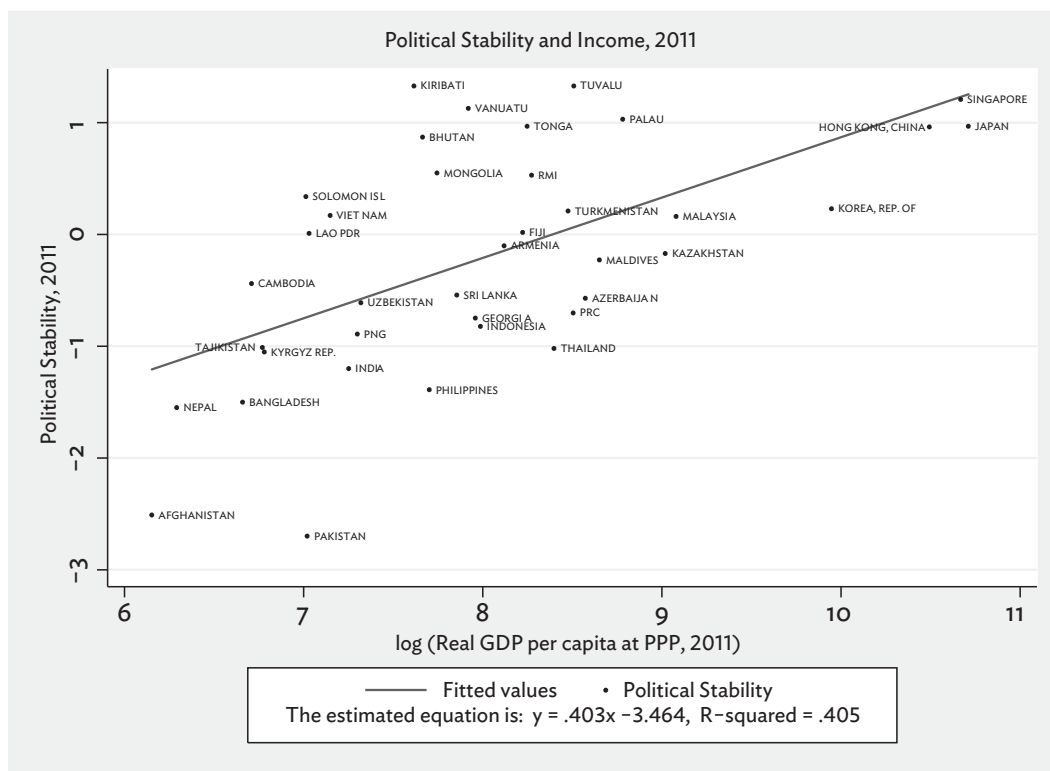
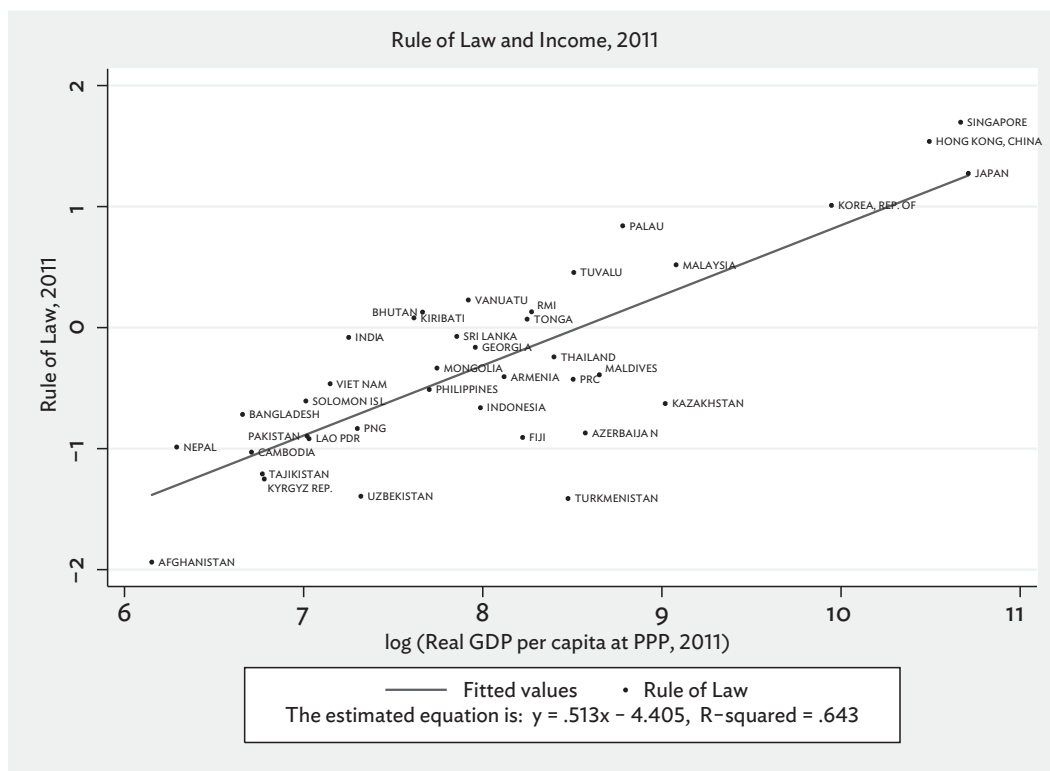
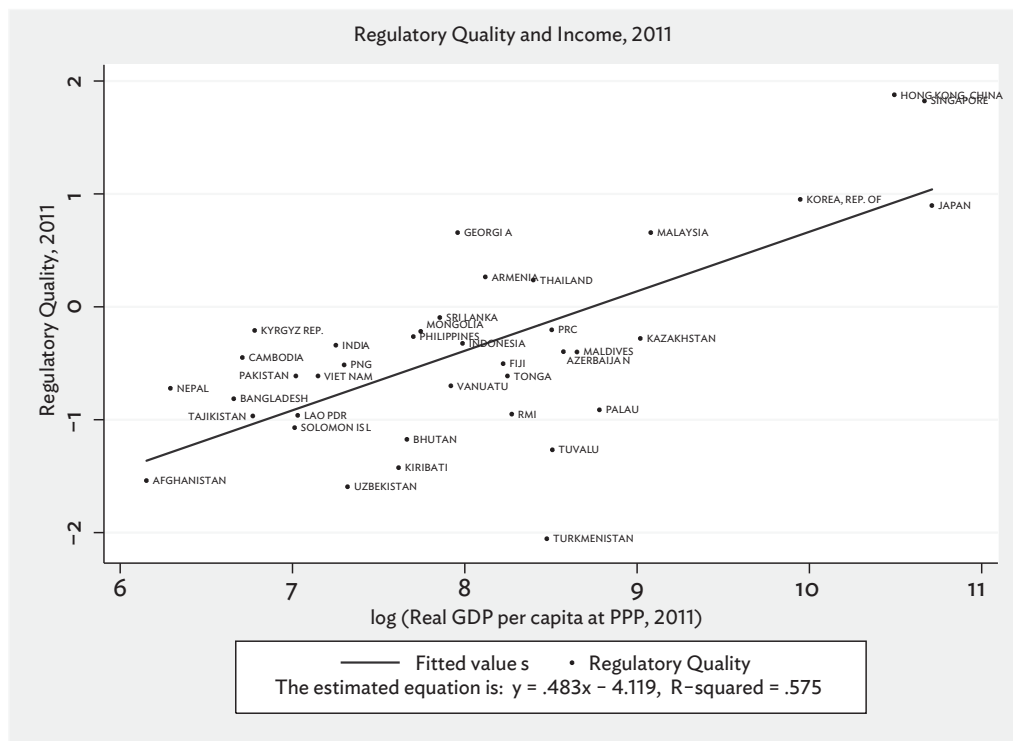
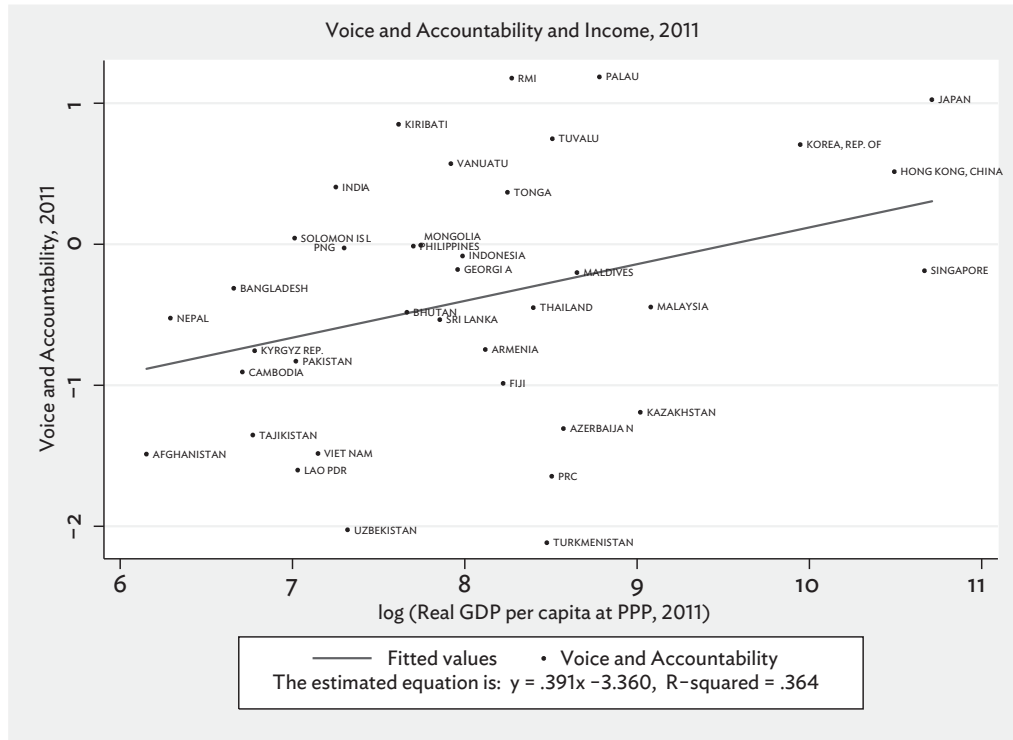


Figure 1: (continued)



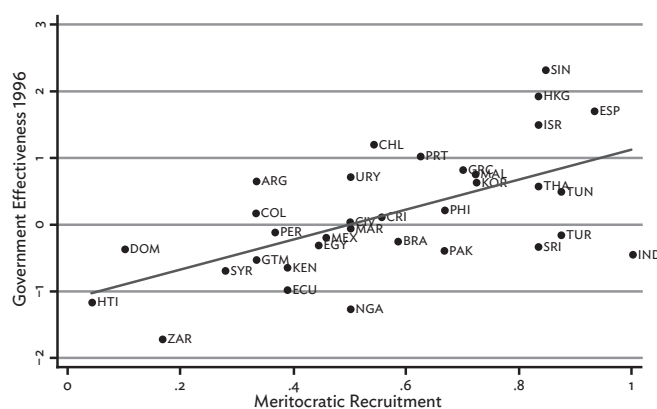
GDP = gross domestic product, PNG = Papua New Guinea, PPP = purchasing power parity, PRC = People's Republic of China, RMI = Marshall Islands.

Source: Author's estimates.

D. Structure of Bureaucracy

Studies by Evans and Rauch (Evans and Rauch 1999; Rauch and Evans 2000) suggest that professional bureaucracy matters for effective governance. Drawing on the original insight of Max Weber (1968), Evans and Rauch argue that the Weberian model of professional bureaucracy contributes to government effectiveness. The key characteristics of the Weberian bureaucracy include meritocratic recruitment, civil service procedure for hiring and firing, and filling higher levels of the bureaucracy through promotion. Figure 2, taken from Baland, Moene, and Robinson (2010), plots the data Evans and Rauch collected on the degree of meritocracy in the bureaucracy against the World Bank's Government Effectiveness Index. It shows that the greater the meritocracy in recruitment, the more effective is the government. Figure 3, also taken from Baland, Moene, and Robinson (2010), plots the degree of Weberianness of the bureaucracy against government effectiveness. Again, there is a positive relationship between the two variables.

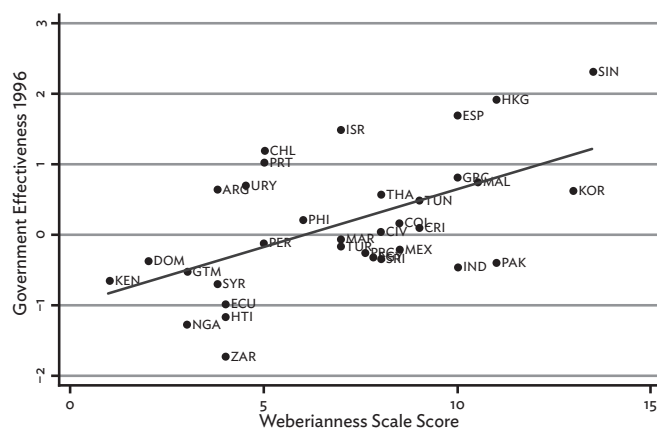
Figure 2: Meritocratic Recruitment and Government Effectiveness



Note: List of corresponding country names in Appendix.

Source: Baland, Moene, and Robinson (2010).

Figure 3: Weberian Bureaucracy and Government Effectiveness



Note: List of corresponding country names in Appendix.

Source: Baland, Moene, and Robinson (2010).

E. Social Capital

There is now a considerable body of literature on the role of social and cultural factors in determining the measures of governance success. According to Putnam (1993), the differences in governance performance between regions of Italy can be primarily explained by their differences in the relative amounts of social capital¹¹—which is interpreted as the degree of social engagements, and trust existing in different regions. Putnam states that trust in strangers helps to foster collective action, which is a requisite for the provision of public goods. Knack and Keefer (1997) and La Porta et al. (1997) also find empirical support for the view that higher social capital, in the form of trust and civic engagement, leads to better governance performance. Drawing on a sample of about 30 nations from the World Values Surveys, they find that higher-trust societies have better government performance (as measured by the surveys of citizen confidence in government and subjective indicators of bureaucratic efficiency).

Collier and Gunning (1999) attribute the poor governance and high incidence of corruption in Africa to its weak social capital, which, in turn, is due to its ethno-linguistic fractionalization and economic inequality.¹² As contrasted from Africa, Asia, on the other hand, exhibits a relatively high level of social capital. Citing the World Values Survey, Zhuang, De Dios, and Martin (2010) suggest that there is a relatively high level of trust among people in East Asia. They also note that after controlling for the level of income, countries such as the PRC, India, Indonesia, and Viet Nam display higher levels of trust than the international average for that income level.

F. Political Economy

Finally, political economy factors have an important influence in determining the quality of governance in a country. Traditional economic theory takes the view that institutions are efficient and they persist as long as social benefits exceed the social costs of replacing them. However, inefficient institutions persist in the real world. This is explained by political economic theories, which attribute institutional changes to distributive conflicts. According to this perspective, institutions and policies are shaped by those in power, who manipulate government policies to control assets and amass resources (see Acemoglu, undated).

There are two types of political power: *de facto* and *de jure*. *De jure* political power stems from the political institutions—i.e., the type of political regime and the constraints it imposes on politicians. However, *de facto* power may be different from *de jure* power, which can be wielded by the bureaucracy, ethnic groups, religions, and lobbies. The distribution of political power—*de facto* and *de jure*—determines the particular kind of political equilibrium that exists in a society, which, in turn, determines the nature of institutions and the quality of governance. It has been suggested that various types of external shocks can lead to a new political equilibrium, changes in the political institutions, and improvement in the quality of governance (Islam 2008).

¹¹ Notwithstanding its popularity and common usage, social capital has remained an elusive concept, as different authors have attached different meanings to it. See Quibria (2003) for a critical discussion of the concept as well as the various measurement and estimation issues associated with its empirical application.

¹² Alesina et al. (2003) find that ethnic and linguistic fragmentation is associated with poor governance, but religious fragmentation is not. Indeed, they find a positive correlation between religious fragmentation and measures of good governance. They argue that this reflects the fact that religious fractionalization tends to be higher in more tolerant societies like the US.

The foregoing discussion should make it clear why governance reform is a complex undertaking for developing economies. First, institutions of governance are path-dependent: some important dimensions of governance are determined by accidents of history and geography. Second, many of the social and cultural dimensions of governance are extremely slow-moving and amenable to little policy intervention. Third, the current state of governance is a reflection of the existing political equilibrium and the distribution of powers in the society. Without upending the power structure, it is difficult to introduce major reforms. Finally, developing countries are severely resource constrained, while major governance reforms are costly.

VI. GOVERNANCE PERFORMANCE OF ASIAN COUNTRIES

A. Performance of Asia and Its Subregions

Although developing Asia has achieved impressive success in economic and social development in recent years, its performance in governance has been somewhat less stellar. This can be seen from Table 4, which reports the WGI for 2011 by region and subregion:

- Developing Asia falls below the global average/median or the Organisation for Economic Co-operation and Development (OECD) average in all six indicators in 2011.
- Developing Asia performs lower than Latin America and the Caribbean in all but one dimension: government effectiveness.
- Developing Asia scores lower than non-OECD countries in three indicators: voice and accountability, political stability, and rule of law.
- Developing Asia, however, fares better than the Middle East and North Africa and sub-Saharan Africa (though all the three subregions perform below the global average in all indicators).

Table 4: Worldwide Governance Indicators by Region/Subregion, 2011

Region/Subregion	Voice and Accountability	Political Stability	Government Effectiveness	Regulatory Quality	Rule of Law	Control of Corruption
Developing Asia	-0.63	-0.98	-0.08	-0.32	-0.37	-0.64
Central Asia	-1.48	-0.52	-0.63	-0.87	-1.05	-1.12
East Asia	-1.51	-0.63	0.18	-0.13	-0.34	-0.55
Pacific	-0.05	-0.58	-0.76	-0.60	-0.79	-0.94
South Asia	0.14	-1.41	-0.23	-0.44	-0.28	-0.67
Southeast Asia	-0.53	-0.73	-0.23	-0.40	-0.56	-0.68
Latin America and the Caribbean	0.15	-0.29	-0.14	-0.06	-0.33	-0.13
Middle East and North Africa	-1.19	-1.20	-0.49	-0.68	-0.57	-0.64
OECD	0.97	0.46	1.18	1.15	1.14	1.05
Non-OECD Europe	-0.49	-0.50	-0.40	-0.21	-0.60	-0.82
Sub-Saharan Africa	-0.70	-1.11	-0.80	-0.66	-0.86	-0.79

OECD = Organisation of Economic Co-operation and Development.

Note: OECD excludes Republic of Korea, which is included in East Asia.

Sources: ADB staff compilation from World Bank: Worldwide Governance Indicators online database; World Development Indicators online database.

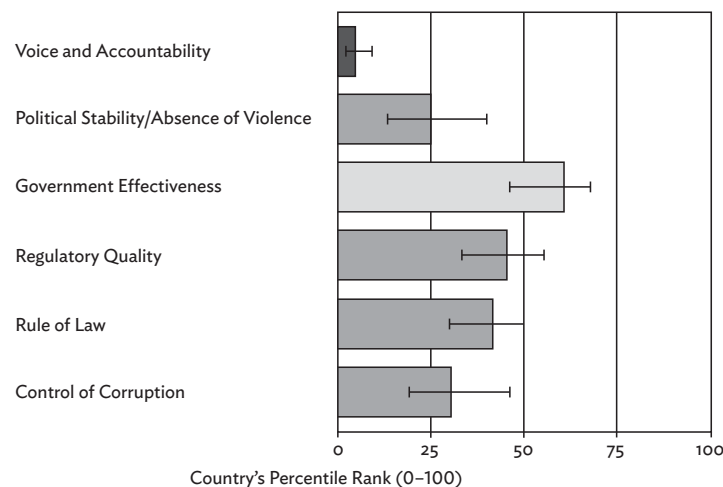
As Table 4 further shows, in governance, a substantial degree of heterogeneity exists among Asian subregions. Some salient aspects of this heterogeneity may be noted:

- East Asia dominates other subregions in government effectiveness, regulatory quality, and control of corruption but performs worst in voice and accountability.
- South Asia performs best in voice and accountability and rule of law but fares worst in political stability.
- Southeast Asia lies in the middle of the pack of the subregions in all indicators. However, its performance in government effectiveness and political stability are respectively the best and the worst among all indicators.
- Compared to other subregions, the Pacific ranks worst in government effectiveness while its performance in other indices lies in the middle of the pack.
- Central Asia ranks the worst in all but categories, which include voice and accountability, political stability, and government effectiveness. Among all the categories, its performance is best in political stability and worst in voice and accountability.

B. Performance of Major Asian Countries

In this section, we consider, for comparison, the governance performance of a select group of countries in Asia: the PRC, India, Indonesia, the Philippines, and Viet Nam. These countries are first assessed by the WGI and then by other alternative governance indicators.

Figure 4: Governance in the People's Republic of China: 2011



Notes: The Worldwide Governance Indicators (WGI) are a research dataset summarizing the views on the quality of governance provided by a large number of enterprise, citizen and expert survey respondents in industrial and developing countries.

These data are gathered from a number of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms.

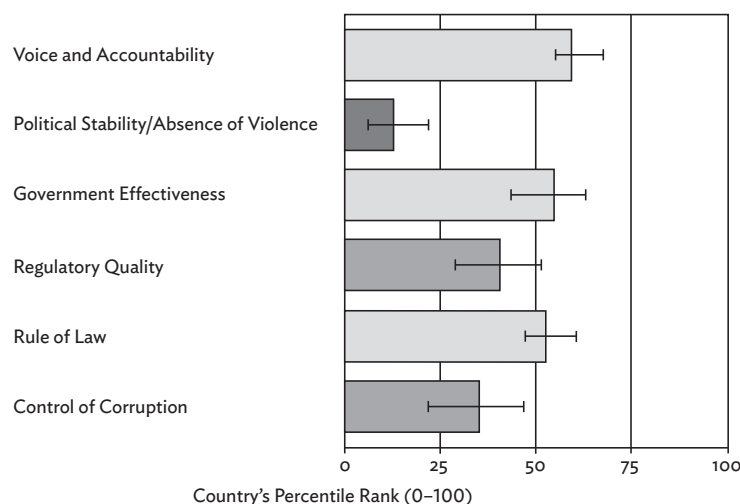
The WGI do not reflect the official views of the World Bank, its Executive Directors, or the countries they represent. The WGI are not used by the World Bank Group to allocate resources.

Source: Kaufmann, Kraay, and Mastruzzi (2010).

People's Republic of China. Except for government effectiveness, the PRC belongs to the bottom half in all other indicators. In voice and accountability, the PRC ranks in the bottom fifth percentile, one of the worst in the world. Its score is lower than that of any in the comparison group. In political stability, it lies in the first quintile, but ranks higher than India (13th percentile) and Indonesia (21st percentile). In regulatory quality, it tops every country in the comparison group, even though all belong to the bottom half. In rule of law and control of corruption, the PRC ranks lower than India. (See Figure 4 for more details.)

India: The country ranks slightly above the bottom half in voice and accountability, rule of law, and government effectiveness. In political stability and absence of violence, it places in the 12th percentile group. In regulatory quality, it belongs in the 40th percentile, below all the countries in the comparison group except Viet Nam. However, in control of corruption, India fares better than all the countries in the group, even though it belongs to the lower 35th percentile. (See Figure 5 for further details.)

Figure 5: Governance in India: 2011



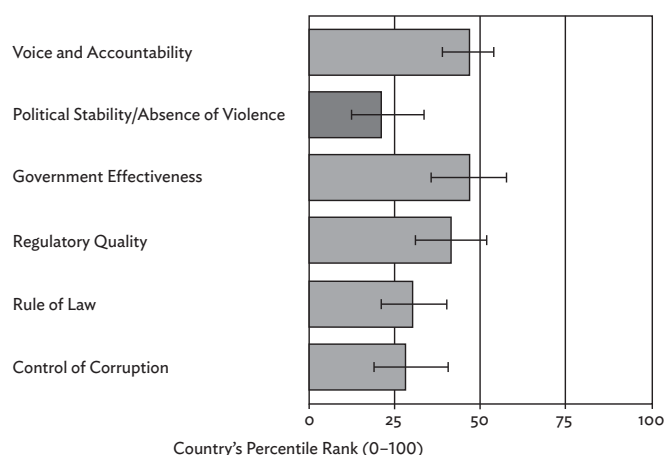
Notes: The Worldwide Governance Indicators (WGI) are a research dataset summarizing the views on the quality of governance provided by a large number of enterprise, citizen and expert survey respondents in industrial and developing countries.

These data are gathered from a number of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms.

The WGI do not reflect the official views of the World Bank, its Executive Directors, or the countries they represent. The WGI are not used by the World Bank Group to allocate resources.

Source: Kaufmann, Kraay, and Mastruzzi (2010).

Indonesia: Indonesia ranks in the bottom half in all indicators of governance. In political stability and absence of violence, it places in the bottom quarter with India and the Philippines. In other indicators, it lies around the middle of the comparison group. (See Figure 6 for more details.)

Figure 6: Governance in Indonesia: 2011

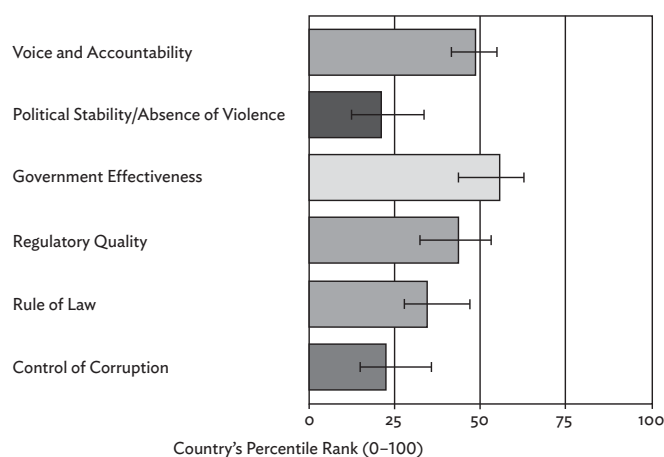
Notes: The Worldwide Governance Indicators (WGI) are a research dataset summarizing the views on the quality of governance provided by a large number of enterprise, citizen and expert survey respondents in industrial and developing countries.

These data are gathered from a number of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms.

The WGI do not reflect the official views of the World Bank, its Executive Directors, or the countries they represent. The WGI are not used by the World Bank Group to allocate resources.

Source: Kaufmann, Kraay, and Mastruzzi (2010).

Philippines: The Philippines is in the bottom half for all indicators except in government effectiveness, where it is grouped in the 55th percentile. In political stability and control of corruption, it is in the first quintile and lies at the bottom of the comparison group. (See Figure 7 for more details.)

Figure 7: Governance in the Philippines: 2011

Notes: The Worldwide Governance Indicators (WGI) are a research dataset summarizing the views on the quality of governance provided by a large number of enterprise, citizen and expert survey respondents in industrial and developing countries.

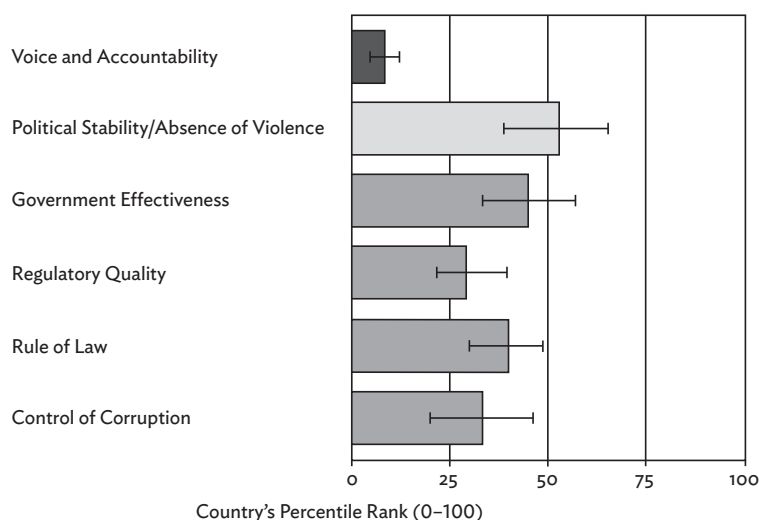
These data are gathered from a number of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms.

The WGI do not reflect the official views of the World Bank, its Executive Directors, or the countries they represent. The WGI are not used by the World Bank Group to allocate resources.

Source: Kaufmann, Kraay, and Mastruzzi (2010).

Viet Nam: Except for political stability/absence of violence, the country ranks in the bottom half. It performs the worst in voice and accountability, where it ranks in the bottom decile with the PRC. (See Figure 8 for more details.)

Figure 8: Governance in Viet Nam: 2011



Notes: The Worldwide Governance Indicators (WGI) are a research dataset summarizing the views on the quality of governance provided by a large number of enterprise, citizen and expert survey respondents in industrial and developing countries.

These data are gathered from a number of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms.

The WGI do not reflect the official views of the World Bank, its Executive Directors, or the countries they represent. The WGI are not used by the World Bank Group to allocate resources.

Source: Kaufmann, Kraay, and Mastruzzi (2010).

How do the above five countries fare in terms of alternative governance indicators? As Table 5 shows, none of the countries exhibit any stellar performance—be it in corruption control, global competitiveness, or the ease of doing business—despite their considerable economic success.

Table 5: Governance Ranking by Alternative Indicators

Country	CPI (2011)	GCI (2012–2013)	Doing Business (2013)
People's Republic of China	80	29	91
India	94	59	132
Indonesia	118	50	128
Philippines	105	65	138
Viet Nam	123	75	99

CPI = Corruption Perceptions Index, GCI = Global Competitiveness Index.

Source: Author's compilation from original sources.

Finally, while the numbers/rankings are suggestive, we should not perhaps read too much into them. In fact, when one looks at them closely, they start to look a bit curious. (See Box 2 for a critical assessment of the PRC's ranking in WGI by Fukuyama [2013]).

Box 2: The People's Republic of China's Ranking in the Worldwide Governance Indicators

There is also something very strange about the Worldwide Governance Indicators rankings of [the People's Republic of] China. [The People's Republic of] China's low rankings for Voice and Accountability and Rule of Law are not surprising, given that no one argues either of these are [the People's Republic of] China's strong suit.

The other four measures relate to what we are defining as governance.

While both the score and ranking for government effectiveness are higher than for any other measure, [the People's Republic of] China still places only in the 60th percentile. In my purely subjective estimation, the effectiveness of [the People's Republic of] China's national government with regard to macroeconomic management of a hugely complex modernization process over the past three decades has been nothing short of miraculous, given the fact that [the People's Republic of] China was not just managing an existing set of institutions, but also transforming them in a more market-friendly direction. Its performance since the Asian financial crisis has arguably been better than that of the United States, which nonetheless ranks in the 90th percentile.

It is not clear whether any of the (WGI) components explicitly seek to measure bureaucratic autonomy. Presumably categories like Political Stability/Control of Violence are exclusively output measures (where [the People's Republic of] China's low 24th percentile ranking seems a bit bizarre). The Rule of Law measure has big problems, beginning with the lack of definition of what is being measured. If rule of law is defined as constraints on the executive, [the People's Republic of] China should rank even lower than it does, as there are no real legal constraints on the behavior of the Chinese Communist Party. If on the other hand this category means something more like rule by law (which would make it a component of governance), the ranking should be considerably higher. Most Rule of Law measures tend to be related to procedures or capacity rather than output, because the output of a legal system is so hard to measure. But we actually have no idea what the Chinese numbers actually mean or purport to measure.

Source: Abridged and reproduced verbatim from Fukuyama (2013).

VII. ASIAN GROWTH PARADOX

A. Reviewing Quantitative Results

It is almost an article of faith in the development community that good governance leads to higher economic growth. Is this expectation borne out in reality in Asian developing economies? This was empirically investigated by Quibria (2006) in the context of a simple model. The exercise involved first deriving an international reference line, which indicates the expected level of governance score against per capita real income. This line is derived by regressing the WGI governance levels of countries against per capita income levels. For this regression, the paper uses a composite governance index, which is the average of all six individual indicators of WGI. The per capita income used for this regression is the "real" income of countries in 2003, which is measured in terms of 2000 purchasing power parity (PPP) dollars. The regression uses data for 151 countries from all over the world for which the governance indices are available for 2002. As expected, the regression line is upward-sloping, indicating that the higher the income level, the better the quality of governance. The international reference line is used to compute countries with "surplus" and "deficit" governance. Countries that lie above the international reference line are considered as having a surplus and those below the international line are considered as having a governance deficit. The paper then goes on to compare the economic growth performance of the governance-surplus countries during 5 years (1999–2003,

for which complete data sets were then available) with the growth performance of the governance-deficit countries. Contrary to expectations, the countries with presumably better governance were found to fare worse in economic growth than those with worse governance. Indeed, the average growth rate of the governance-surplus countries was less than half that of the governance-deficit countries. Moreover, the governance-deficit countries had a lower variance in their growth rates (at 0.1) than the governance-surplus countries (at 2.6).

How does one explain this seemingly paradoxical result? One conjecture is that this is largely due to what economists call *convergence*—that is, poor countries tend to grow faster than richer countries. However, on the face of it, it does not seem particularly plausible, as both groups include an assortment of countries at different stages of development with different income levels. To investigate the question more rigorously, the paper next estimated a parsimonious growth equation as follows:

$$gdp\ growth = a + b (\ln\ gdp\ per\ capita) + c\ (governance) + errors,$$

where a , b , and c are the parameters to be estimated. The regression involved 29 Asian countries for which relevant data were available. The estimated equation yielded a significant coefficient for governance but with the wrong sign.

In a recent study, Zhuang, De Dios and Martin (2010) revisited the paradox. However, they took a more disaggregated approach. Rather than taking a composite index of governance, they considered all the six components of the WGI separately. They also extended the dataset to 1998–2008. This study seems to suggest that the governance–growth paradox is still salient in Asia: regressing the annual average GDP growth rate against the six indicators separately (controlling for initial income), they found that except for voice and accountability, which had a statistically significant negative coefficient, other governance indicators did not have statistically significant coefficients.¹³ Statistical quibbles aside, the larger point that emerges from this discussion is that the data do not provide any robust evidence of a tight governance–growth relationship in Asia.

In this connection, it may be noted that the growth–governance paradox in Asia is now widely recognized in the economic profession. According to Rodrik (2008, p.19):

[T]here are enough countries that are growing rapidly despite poor governance—[the People’s Republic of] China, Viet Nam, Cambodia to name some of the prominent Asian examples—to render suspect any general claim to the contrary. Indeed, we should take it as good news that large-scale institutional transformation—of the type entailed by the governance agenda—is hardly ever a prerequisite for getting growth going.

B. A Case Study of Bangladesh

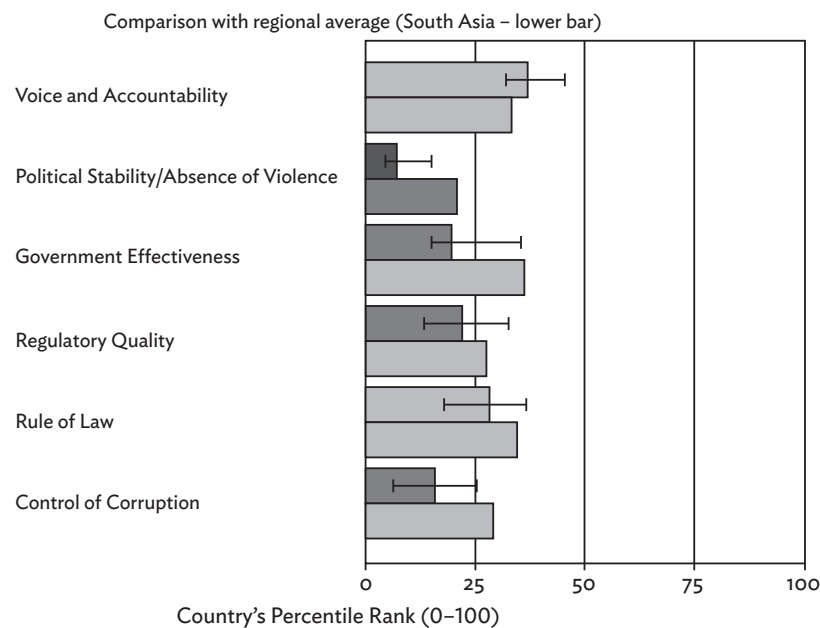
Asia has many examples of countries that have done well with poor governance. One interesting case is Bangladesh. Since its independence in 1972, the country has improved its economic growth performance in every decade and has grown at around 6% since the 1990s. In the past decade, it has reduced its poverty by one-third. Its success in social indicators is equally commendable. Bangladesh increased its life expectancy from age 59 to 69 between 1990 and 2010. The country has achieved universal primary enrollment, accomplished gender equality in primary and secondary education, and

¹³ See footnotes 15, 16, and 17 in Zhuang et al (2010).

reduced child mortality by two-thirds since 1990. Even though Bangladesh has half the income of India on a per capita basis, it outperforms India in almost all social and human development indicators (Dreze and Sen 2011).

However, by the WGI measures, Bangladesh ranks in the bottom quintile or slightly above it, except for voice and accountability, comparing unfavorably with countries in South Asia (see Figure 10). Similarly, according to the CPI ranking of Transparency International, it lies at the bottom or near bottom. Notwithstanding these putative governance failures, the country has made significant gains, even better than those with better governance. How does one explain this paradox? See Box 3, which reproduces a commentary by Devarajan (2008), for an answer.

Figure 10: Governance in Bangladesh: 2011



Notes: The Worldwide Governance Indicators (WGI) are a research dataset summarizing the views on the quality of governance provided by a large number of enterprise, citizen and expert survey respondents in industrial and developing countries.

These data are gathered from a number of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms.

The WGI do not reflect the official views of the World Bank, its Executive Directors, or the countries they represent. The WGI are not used by the World Bank Group to allocate resources.

Source: Kaufmann, Kraay, and Mastruzzi (2010).

Box 3: It's the Data, Stupid!

The Bangladesh governance paradox has been the subject of a good deal of discussion in the development community. This disjunction between governance and growth in Bangladesh has much to do with the coarseness of governance data which fail to capture the richness of country-specific detail, embedded in the country's historical, political, and cultural dimensions. Devarajan (2008) explains the governance conundrum in Bangladesh in the following way:

(First), governance indicators in Bangladesh fail to capture the fact that the country has a vibrant and active civil society that not only delivers services, but provides some accountability to government. The WGI also seems to overlook the increasingly mature media, including vernacular newspapers, which plays something of a watchdog role.

(Second), the relation between governance and development in Bangladesh is unique, because the Bangladeshi people have worked around the country's governance problems to spur development. When the country was born, out of a civil war, there was hardly a government. International and national nongovernmental organizations (NGOs) filled the vacuum by delivering basic services, such as health, family planning, and education, and by creating microcredit schemes. As these efforts proved effective, the government made space for these NGOs and the private sector, in some cases contributing to their financing. The government funds secondary education, for example, although 95 percent of it is provided by the non-state sector. Similarly, Bangladesh's garment export sector grew rapidly, thanks to duty drawback systems and bonded warehouses that enabled textiles to come into the country duty-free, circumventing a highly opaque customs system. Of course, this explanation does not explain why Bangladesh was able to work around its governance problems when so many other countries were not.

(Third), Bangladesh is a densely populated, homogeneous society, in which innovations spread like wildfire. Soon after one village discovers something that works, neighboring villages find out about it and adopt it. As a result, family planning, microfinance, and other programs took off in Bangladesh more easily than they might have elsewhere. By the time the government grew strong enough to control the NGOs and others, it was too late, as microfinance, family planning, and private schooling had already become commonplace.

Although Bangladesh is a particular case, it highlights some general issues with the Worldwide Governance Indicators data, which were succinctly summarized by Devarajan as follows:

The Bangladesh case illustrates the fact that governance indicators such as the WGI do not capture the multifaceted ways in which governance affects development in a particular country. It would be dangerous to use indicators to jump to simple conclusions without understanding the specific relation between governance and development in a particular country; the indicators should certainly not be used by themselves to design policy responses to problems of weak governance. This is the downside of having an indicator that permits inter-country comparisons of governance: the richness of country-specific detail is lost.

Source: Abridged and reproduced verbatim from Devarajan (2008).

C. Explaining the Paradox

One can think of a number of possible explanations for the apparent paradox. First, the literature highlights a number of measurement problems with respect to the WGI data, which include definitional issues, exclusive reliance on perceptions, biases in expert assessments, correlated perception errors, and question of comparability across countries. These measurement errors make the data inadequate for capturing the nuances of the growth–governance nexus.

Second, it is possible that some aspects of governance are more important than others at a particular stage of development. It is not the overall aggregate score in a particular category of governance that is salient, but rather its particular dimension. For example, it may not be the incidence or the volume of corruption that is most relevant. It may be the organization of corruption—whether

centralized or decentralized—that matters for growth (or lack of it). Shleifer and Vishny (1993) have noted that a decentralized system of corruption (where bribes are paid separately for 10 different signatures from 10 different agencies) is economically more harmful than a centralized system of corruption (where all bribes are coordinated through a “one-stop shop” for 10 different signatures). The existing WGI data are too coarse to capture such distinctions.

Third, most developing countries operate in a mixed environment of formal and informal institutions. However, a country’s score is based on an implicit model of governance that exists in advanced western countries. The larger the gradient of the state of governance institutions from the western model, the lower is the score. However, the process to initiate and sustain growth in a low-income country can be very different from that of a middle- or high-income country. In such an environment, informal, self-enforcing, relationship-based governance (as opposed to a formal, rule-based system) can work efficiently and produce large growth payoffs. The advantage of the informal relation-based system is that it has little or no fixed costs whereas the formal system requires substantial fixed costs to legislate the law, and establish the courts to adjudicate disputes and police force to enforce a court verdict (Dixit 2009). The informal system in Southeast and East Asia is pervasive; it has been sustained by its high social capital—in the sense of trust (Zhuang, De Dios, and Martin 2010).

VIII. CONCLUSIONS: REFORM AGENDA FOR DEVELOPING ASIA

The earlier discussion suggests that most Asian developing countries do not rank high in the existing indicators of governance. This partly reflects measurement issues—how data are collected and collated—as well as the bias inherent in the implicit model of governance that defines the metric of measurement. For example, in parts of Asia, many contractual arrangements are informal and relations-based, or political institutions are insufficiently open or participatory. Admittedly, the existing institutions of governance did not garner these countries high points on the existing governance scale. Nevertheless, these deficiencies have not blocked these countries from achieving remarkable economic success. This success begs the question: Is there any rationale for governance reform in Asia?

The rationale for future reform is twofold: First, as Asian economies grow and economic transactions become more complex, there will be greater strains on informal and inefficient institutions; this will warrant a move toward a more efficient, formal institutional arrangement. This move—in the form of rule of law, effective government, or good regulation—will be essential to generating robust and sustained economic growth. Second, good governance—in the form of transparency, accountability, voice, or lack of pervasive corruption—is an attribute of a good society. As developing Asia climbs the economic ladder, there will a greater demand for good governance in the form of more transparent, open, and inclusive institutional arrangements.

The above remarks should not be interpreted to imply that the reform agenda will be identical across countries. While there may be some common elements, the reform agenda—its content and sequence—will vary across countries for three reasons. First, if the available data are any indicator, Asian countries are heterogeneous in terms of the nature and extent of governance deficits. An agenda of reform needs to take into account this heterogeneity in initial conditions. Second, different societies, based on their history, traditions, and politics, are likely to attach different weights to different elements of good governance. Finally, societies are different in their capacities to design appropriate institutional arrangements, which require local knowledge and creativity (Rodrik 2008). This also

explains why cherry-picking best practices and institutions and transplanting them across societies do not work. In sum, there is no one-size-fits-all solution.

In designing the reform agenda of a country, the following considerations would be salient. First, the country needs to be selective and strategic. The reason for selectivity stems from the fact that developing countries have limited budgetary and human resources that constrain their ability to undertake large-scale governance reforms: every peso spent on judicial reform to improve the rule of law cannot be spent on such public goods such as health, education, and physical infrastructure (Posner 1998). The reform agenda should be strategic in the sense that it should emphasize items that yield the biggest bang for the buck—be it in the form of welfare improvements or productive efficiency.

Second, the country needs to avoid the pitfalls of random—or hit-or-miss—reform. Some reform can look good in isolation but can have unintended consequences. This is illustrated by the institutional version of the theory of the second best (Stephenson 2007). As is well known, the theory of the second best suggests that in a world of multiple distortions, correction of a single distortion may lead to a reduction in welfare. A simple generic institutional version can be applied to the question of the optimal autonomy of the bureaucracy. The quality of the government depends on the efficiency of its bureaucracy, which is determined by its *capacity* and *autonomy* (Fukuyama 2013). The former relates to its education and professionalism, while the latter refers to its autonomy to make independent decisions without being micromanaged. In countries with a capable bureaucracy, the first-best standard is to allow it greater bureaucratic discretion in decision making. However, when the bureaucratic capacity (professionalism) is lacking, permitting more discretion is worse than a situation of less discretion—i.e., little autonomy with well-defined rules. In other words, allowing a venal bureaucracy more discretion to judge “case by case” may simply result in “suitcase by suitcase,” as felicitously described by Bardhan (2006). This issue of the theory of the second best also applies to many other areas of governance, including judicial reform (Stephenson 2007).

Third, in initiating and sustaining reform, political economic considerations are critical (Islam 2008). Reform creates winners and losers; good economics is often bad politics. To initiate and sustain a reform agenda, political equilibrium needs to be changed in its favor. This change can take place due to external shocks—such as wars and economic crises; the pressure of powerful external agencies that have an influence on the body politic; or the internal social dynamics, stemming from the pressures of an organized and conscious civil society and the media.

Finally, even though the provenance of institutional innovations is always invariably domestic, there are things that international organizations can do to improve the quality and nature of existing institutions. One low-hanging fruit of governance concerns openness and transparency of policy making (Acemoglu 2008). A policy of openness and transparency is not particularly intensive in human and fiscal resources. Nor does this appear to have any unintended adverse consequences. On the other hand, such a policy can be a powerful antidote to corruption that is endemic in many Asian countries (as corruption is in large part due to the close and nontransparent manner policies are formulated and implemented). Though transferring best practices and institutions may be a fool’s errand for international organizations, advocacy of the principles of openness and transparency is not.

APPENDIX: LIST OF ECONOMIES

Economy	Code
Argentina	ARG
Brazil	BRA
Chile	CHL
China, People's Republic of	PRC
Colombia	COL
Congo, Dem. Rep. of	ZAR
Costa Rica	CRI
Côte d'Ivoire	CIV
Dominican Republic	DOM
Ecuador	ECU
Egypt	EGY
Greece	GRC
Guatemala	GTM
Haiti	HTI
Hong Kong, China	HKG
India	IND
Israel	ISR
Kenya	KEN
Korea, Republic of	KOR
Malaysia	MAL
Mexico	MEX
Morocco	MAR
Nigeria	NGA
Pakistan	PAK
Peru	PER
Philippines	PHI
Portugal	PRT
Singapore	SIN
Spain	ESP
Sri Lanka	SRI
Syria	SYR
Thailand	THA
Tunisia	TUN
Turkey	TUR
Uruguay	URY

Source: Evans and Rauch (1999).

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Governance and Developing Asia:

Concepts, Measurements, Determinants, and Paradoxes

This paper provides a critical review of this literature, which brings into the open a number of serious conceptual, measurement and data issues, as well as the existence of an Asian governance paradox. This paradox calls into question the quality of the existing data and the analytical basis of the policy orthodoxy, which seems to be essentially faith-based.

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