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An Exploratory Study on the Relationship of Public Governance and Ease of Doing Business

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Abstract

Purpose of the study is to explore the relationship of the practice of good public governance in governmental institutions on the performance of the government in terms of its ease of doing a business. The motivation of the study was driven by the fact that each country has different easy of doing business performance even though they are located in the same region. Furthermore, massive competition among countries to attract foreign capital inflow is justification that the research is relevant to be conducted. Easy of doing business is a fundamental factor that determines foreign investor regarding their investment decision. The study examines whether good public governance practice in governmental institutions will have positive implication to government performance in terms of its ease of doing business. The study applied exploratory research design, in which two independent variables were examined. Public governance and easy of doing business performance are two independent variables as an object of the investigation. Indicators namely public accountability, effectiveness government, control of corruption, political stability, regulatory quality and rule of law are a representation of the public governance independent variable. Governance index namely World Governance Index was used for the purpose public governance measurement. Meanwhile, Easy of doing business performance was measured using Index released by World Bank. The total sample was involved including 188 countries of World Bank members. The data was analyzed using bivariate correlation. The findings indicate that all indicators of public governance show positive and significant correlation with ease of doing a business performance. The correlation magnitude shows that majority of public governance indicators have a strong correlation ($r > 0.6$, $p<0.01$). Meanwhile, political stability shows moderate correlation ($r = 0.584$, $p<0.01$). The result implies that if the government adopts good public governance principles in public administration, it may have the positive impact on government performance in terms of ease of doing business.

Keywords

Ease of doing business; Foreign Direct Investment; Governance; World Governance Index

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Introduction

During the last decade, good governance has become a topic of great interest among scholars and public sector managers, especially starting from the premise that good governance influences economic prosperity (Knack and Keefer, 1995, Ngobo and Fouda, 2012, Mauro, 1995). Good public governance has been identified by academicians, donor institutions, policymakers and civil society organization as a pivotal factor for national development (World Bank Institute, 2009). Constructing good governance is the never-ending process and the nation build with good governance principles is believed can lead the state toward economic prosperity

The country with a simple procedure in terms of doing business will attract investor both local and international to spend their capital in the business sector. The role of government in streamlining procedure of doing business is very crucial. In order to increase easiness of doing a business performance, the government and the public sector must put a major concern on efforts in simplification of business regulations that inhibit activities of doing business or opening new business (Bota-Avram, 2014). Effective governments should properly answer to citizen needs, promote politically neutral managers, and develop a framework of pro-business policies (Andrews, 2008).

Public governance, in general, is related to the making of the public decision and its implementation (OECD, 2011). The countries that practice good public governance usually adopt principles such as flexibility, guidance, communication, and persuasion rather than rigid traditional "control and command" approaches (OECD, 2011). Public governance is important for investors as basic requirement regarding country risks. Stability of the government is needed for investment planning both medium and long-term. Public Governance by many scholars is closely associated with the easiness of doing business (Bota Avram, 2014, Ngobo and Fouda 2012, Çule and Fulton (2013) and poor public governance is believed as a major problem of economic development (Ngobo and Fouda (2012). Good governance leads to a transparent environment for conducting public affairs, being a promoter of free-market policies, justice, and the rule of law (Ngobo and Fouda, 2012). Good governance implies fair regulatory frameworks, accountability, and transparent policymaking, all these factors having direct influences on economic activity (Bota-Avram, 2014).

Public sectors and private sectors have symbiosis mutualism in terms of motivation in achieving their objectives efficiently. Private sector expects that public sector supports them by facilitating regulatory that friendly to business organization and clean bureaucracy from corrupt behavior (Bota-Avram, 2014). The rationale of public governance influencing the business environment is based supposition that control toward corruption is expected to drive economic performance through reducing high-cost economy (Çule and Fulton (2013).

Academician, bureaucrats, and business profession are inconclusive that FDI inflows are determined by the host country's factors such as bureaucracy, regulatory, efficient legislatures and transparent judiciaries, (Alemu, 2013). Many governance studies have proved that the quality of public governance has a positive relationship with effectiveness economic resources allocations, which finally influence the stimulation of economic growth and the competitiveness of business environment.

(Price et al, 2011. It implies that institutions are important for economic growth (Keefer and Knack (1997). Research findings revealed that the government institutions played an important role in the economic success and growth in East Asia (Rodrik, 1997). Good governance increases FDI inflows (Globerman et al, 2006) and all governance indicators indicated to have a positive and significant influent toward the level of FDI inflows (Bissoon, 2012).

Good Public governance institutions have the capacity to facilitates benefits for private sectors to grow. Tax incentive, fair legal system, and property right protection are kind of outcome produced by good public governance practice that can foster business organization (Johansson 2001). Good public governance practice encourages investment environment and at the end will generate economic growth Globerman and Shapiro (2003). Differences in Growth and productivity across countries are determined by its governance infrastructure (Kaufmann, Kraay, Zoido, Lobaton, 1999b).

World Bank defines determinants of public governance into indicators namely public accountability, government effectiveness, control of corruption, rule of law, regulatory quality and political stability. Most studies conclude that public governance had a positive impact on Foreign Direct Investment (FDI) and easiness of doing business. However, detail information about attributes of public governance affecting FDI and easiness of doing business is still not revealed clearly.

Literature and Hypothesis Development

Public Accountability and Ease of Doing Business

Public accountability refers to government capacity to respond society in terms of political process, civil liberties, and political rights (Bota-Avram, 2014). It covers participation of the citizens in terms of selecting the government (Alemu, 2013). Public accountability reflects the involvement of the citizen in running the government through their voice in general election. The government, as representative of the citizen, therefore must be accountable to a citizen for every policy taken. The countries with high score index voice and accountability indicate that those countries are countries that put a weight the democracy.

Public accountability facilitates friendly investment climate (IADB, 2001, Siddharthan, 2009). Research findings by Globerman & Shapiro (2002) and Méon, P.G. and K. Sekkat (2007) indicated that public accountability contributes positively to rising FDI inflows. One of the crucial factors that determine the magnitude of FDI inflows is a simplification of investment procedures. Since there is a logical relationship between public governance, FDI and investment procedure. Formulation of the hypothesis is:

Hypothesis 1: The higher public accountability Index, the higher of ease of doing business performance will be

Regulatory Quality and Ease of Doing Business

Regulatory quality refers to how the state manages the rules for general interest including business activities among private sector organization (Rhodes, 1997. It includes government capability to provide regulations that drive business organization growth (World Bank Institute, 2009). High regulatory quality prevents the maters that are identified as a barrier to growth such as government control toward price, lack of financial access and complex regulation (Bota Avram, 2014). Regulatory quality is determined by government efforts in eliminating market policies that are not in favor of business organization such as market controls, limitation on capital movement and government intervention, (Fazio and Talamo, 2008). Quality of regulations, credible government institutions, and public accountability are identified as fundamental factors that influence success of economic growth (Kray and Tawara, 2010) and Bota Avram, 2014)

Clarity and certainty of the regulation are considered by businesses organization regarding its investment decision (OECD, 2011). Government regulations which support the creation of a business-friendly environment, innovation and competitiveness can enhance business performance (OECD, 2011). Meanwhile, poor government regulation will slow down business responsiveness, divert resources and can potentially hamper business initiation. The quality of regulation was found significantly influence the investment climate (OECD, 2011). Formulation of the hypothesis is:

Hypothesis 2: The higher regulatory quality index, the higher ease of doing business performance will be.

Rule of Law and Ease of Doing Business

A country with high rule of law index has characteristic that its society have confidence about law enforcement by the government. It is indicated with the condition such as effective and predicted of the judiciary system and the law enforcement (Bota-Avram, 2014). Rule of law is very important for the company that is doing business in the certain country. Without any rule of law enforcement, they will face any kind of uncertainty or risk regarding their business. Piracy of product is an example of common threats faced by the business organization. They need some assurance that their product innovations are protected by rule of law. Innovations growth can be enhanced if rule of law that regulates protection of intellectual properties right is enforced (Alemu 2013)

Rule of law of the country will be a fundamental factor considered by foreign investor regarding long-term orientation investment (Hoff and Stiglitz, 2005). The country with rules of law more favorable to business entities will get more priority from venture capital to invest their money. Good governance must necessarily ensure a framework of good rules that clearly establish and clarify property rights, rules that are meant to enhance the predictability of economic interactions between various contractual partners (Bota Avram, 2014). İnvestor confidence about rule of law of the country is believed as a most important aspect that influences investment decision (OECD, 2011). A study by Johnson et al (1998) shows that the unofficial economy is positively influenced by the existence of more corruption and when the rule of law is weaker. Formulation of the hypothesis is:

Hypothesis 3: The higher rule of law index, the higher ease of doing business performance will be.

Effectiveness Government and Ease of Doing Business

Government effectiveness refers to the capability of the government in providing good or excellent public services with sufficient sources of economic input. Quality of public services is the main indicator to measure government effectiveness (World Bank Institute, 2009) In achieving the effective government, it will be determined by factors such as civil servants competency, the degree of bureaucracy, independent public services form political influence and the government credibility (Bota Avram, 2014). Effective government enables to attract foreign investors due to simplification of bureaucracy, procedures and time needed to complete all activities regarding investment (IADB, 2001; OECD, 2002). Effective government is important for the business organization because it can lead to a reduction of transaction cost.

Societal issues emerge when the normative function of government and economic institutions is not properly working (Kooiman, 1999). The effective government provides a high quality of public service, simple bureaucracy and credible (Alemu 2013). The capability to implement policies that are beneficial to society including business organization is the outcome of effective government (Rammal and Zurbruegg, 2006) and its important determinants of foreign investment inflow (OECD, 2011). Sedik (2012) who studies on MENA countries found that FDI inflows are positively and significantly influenced by the government effectiveness. Formulation of the hypothesis is:

Hypothesis 4: The higher effectiveness government index, higher performance of ease of doing business will be.

Political Stability and Ease of Doing Business

Political stability promotes confidence to attract foreign direct investment to the host country (Alemu, 2013). Political stability refers capability of the government to maintain conducive domestic political situation and protect the government in power from the potential threat of unconstitutional political movement (Bota Avram, 2014). The influence of political factors in the process of governance should not be ignored. The domestic political situation will determine the orientation and priority of the country in terms of management of the government.

Stasavage (2002) found that there is a strong correlation between the existence of political stability and the foreign investment inflows. Political

Stability is a fundamental factor that ensures sustainability of MNCs staying in the certain country and attracting Foreign Direct Investment (IADB, 2001). The investor will consider the sustainability of business for long term. İt is, therefore, political stability of the country is a fundamental factor as consideration among foreign investor (Fazio and Talamo, 2008). MNCs avoid doing business in the country with the high profile of political risk and tend to move to a country with stable political condition (Meyer, 2005). A study by Amal et al (2010) indicated that stability of political condition of the country has a positive and significant correlation with FDI inflows. Formulation of the hypothesis is:

Hypothesis 5: The higher political stability index, the higher of ease of doing business performance will be

Control of Corruption and Ease of Doing Business

Corrupt behavior in governmental institutions harms not only state finances but it also causes business organization facing high-cost economy (Alemu, 2013). Corrupt bureaucrats usually use their power to charges the business organizations with unregulated various costs. By reducing red tape and corruption behavior in government institutions it can enhance FDI (Vittal (2001). Corruption in governmental institutions can reduce national competitiveness ass well business organization in that country (OECD, 2011). İmpact of corruption in government bureaucracy is similar to excessive taxes charged to a business organization that leads to the hesitation of the foreign investor. Bureaucratic regulations are frequently found as motive among corrupt bureaucrat to charge business institutions (Alam, Mian, and Smith, 2006).

Pervasive corruption causes business organization suffers inefficient economy and ambiguity feeling about the future return. A higher fiscal burden and a high level of corruption are strongly associated with larger unofficial economies (Friedman et al. (2000). Combating corruption, reducing complex bureaucracy and providing efficient government are a fundamental aspect that determines FDI inflows (Méon and Sekkat, 2005). The effects of corruption are significant on economic growth and investment (Mauro, 1995). It effects on public investment cannot be ignored while they are quite significant (Tanzi and Davoodi,1997). Corruption influences negatively the attractiveness for international investors (Wei, 2000). Formulation of the hypothesis is:

Hypothesis 6: The higher control of corruption index, the higher easy of doing business performance will be

Methodology

The exploratory research approach was used in this study. A limited similar study previously conducted and lack of firm theory as a basis for justification the proposed hypothesis are consideration of using exploratory research design. There are two independent variables involved in this study namely public governance and ease of doing a business performance.

Measurement of Public governance variable referred to World Bank Organization. World Bank defined

Public Governance into six indicators namely public accountability, regulatory quality, rule of law, the effectiveness of government, political stability and control of corruption. Those six indicators of public governance in this research was treated as sub independent variables of Public Governance.World Governance Index (WGI) released by World Bank was used to measure Public Governance Variable. WGI is stated in intervale scale range from -2.5 (minimum) to +2.5 (maximum). The higher WGI index is indicating the better Public Governance Practice.

Meanwhile, variable ease of doing business performance was measured using Distance to Frontier (DtF) score released by World Bank. The distance to frontier score benchmarks economies with respect to regulatory best practice, showing the absolute distance to the best performance on each Doing Business indicator (World Bank, 2018). Distance to Frontier is stated in intervale scale range from 1 (minimum) to 100 (maximum). The higher score of Distance to Frontier index, it indicates that the country has the higher easy of doing a business performance.

This research used secondary data namely Worldwide Governance Index (WGI) and Easy of doing business index measured using Distance to Frontier (DtF) score. The data is both released by World Bank Organization. The data is an open publication and it was collected from the website of World Bank. The data is the publication of WGI and Dtf for the year of 2015. The sample of the study is countries listed as a member of World Bank Organization. The total sample was involved in this study is 188 countries of 214 countries. The research used Purposive sampling method in terms of determining the samples. The consideration of using purposive sampling method is representation and matching data. The data must represent five continents. Furthermore, the data of WGI and Easy of Doing Business must be fit in terms of the year of investigation.

The analysis used descriptive statistics approach along with bivariate correlation analysis. Purpose of using descriptive statistic is to understand basic features of the data such as minimum value, maximum value, mean and standard deviation. Meanwhile, bivariate correlation analysis was intended to understand the association between two variables that stand independently. The using of bivariate correlation was also addressed to justify whether the proposed hypotheses are accepted or not. Due to the data is on interval scale categorization, Pearson correlation was used in this research

Results

Descriptive Statistic

World Governance Indicator released by World Bank is stated in interval range, it scales from the minimum value of -2.5 (Worst) to +2.5 (best). Information in Table shows that public governance attributes of 188 countries as a sample of the research are at under moderate value (WGI=0) It is indicated by an average of mean value equal to -0.0534. Mostly, the countries that are indicated having WGI above average are countries with high Gross Domestic Product. Interestingly, most of them are Scandinavian countries.

Top ten of highest WGI in this research in New Zealand (1.87), Switzerland (1.80), Norway (1.77), Finland (1.77), Sweden (1.75), Denmark (1.72), Luxembourg (1.72), Netherland (1.66), Canada (1.64) and Singapore (1.60). Meanwhile, the countries identified as the lowest WGI index is majority characterized as under developing countries and countries familiar with conflict. Top ten of the worst WGI score is South Sudan (-1.88), Syrian Arab Republic (-1.84), Libya (-1.81), Central African Republic (-1.61), Sudan (-1.61), Republic Yemen (-1.59), Eritrea (-1.56), Democratic Republic Congo (-1.54), Afghanistan (1.49) and Iraq (1.47).

Standard deviation as depicted in Table 1 indicated that the value is relatively high (0.96688). It implies that the sample involved in this research is heterogeneous in terms of variation of WGI index. The high standard deviation can be also interpreted that the data is a representation of population (normally distributed). There are 79 countries (42%) with WGI score between 0 to +2.5 and 99 (58%) countries with WGI score between 0 to +2.5. The distribution of WGI score is dominated by countries with WGI performance below average (WGI=0). It implies that practice of good public governance globally is still underdeveloped. Referring to top ten of highest WGI score performance and top ten the worst WGI score performance, efforts to improve economic condition and avoid conflict both internal and external may be one of the solutions to improve public governance index level.

Table 1. Descriptive Statistic of Public Governance and Ease Doing Business

No	Variables	N	Minimum	Maximum	Mean	Std. Deviation
1	Public Accountability	188	-2.04	1.70	-0.0210	0.96283
2	Effectiveness Government	188	-2.17	2.25	-0.0513	0.97849
3	Regulatory Quality	188	-2.24	2.26	-0.0295	0.95686
4	Control of Corruption	188	-1.83	2.29	-0.0674	0.97960
5	Rule of Law	188	-1.99	2.07	-0.0535	0.96065
6	Political Stability	188	-2.94	1.49	-0.0976	0.96286
	AVERAGE				-0.0534	0.96688
7	Easeof doing business	188	26.40	86.70	60.2879	13.07213

World Bank developed ease of doing business index using Distance to Frontier (Dtf) interval scale from 0 (worst) to 100 (best). Information from Table 1 shows that ease of doing the business of 180 countries has a mean value equal to 60.2879. It can be identified that performance of ease of doing business is on a moderate level. Meanwhile, standard deviation indicates on high-level (13.07213). It implies that the variation value of ease of doing business is relatively high. High standard deviation means that the samples have heterogeneity in terms of ease of doing a business performance. It implies that the countries included in the research have characteristic both in extremely good and extremely bad in terms of their ease of doing a business performance.

Correlation Analysis

Bivariate correlation analysis was applied in order to understand the degree of the relationship between two independent variables. Summary of bivariate correlation results is presented in table 2 as follows:

Table 2. Correlation Matrix

No	Variable	1	2	3	4	5	6	7
1	Public Accountability	1						
2	Government Effectiveness	0.681*	1					
3	Regulatory Quality	0.701*	0.935*	1				
4	Control Corruption	0.754*	0.907*	0.868*	1			
5	Rule of Law	0.763*	0.944*	0.929*	0.953*	1		
6	Political Stability	0.709*	0.676*	0.633*	0.747*	0.736*	1	
7	Easiness Doing Business	0.606*	0.865*	0.881*	0.744*	0.816*	0.584*	1

**Correlation is significant at the 0.01 level (1-tailed).*

In this research, the examination of correlation procedure is one way and it refers to positive direction. The consideration of using one-way correlation analysis is due to availability sufficient literature that can be used as the basis for justification of relationship between two independent variables, in this case, public governance and ease of doing business. The correlation results between independent variables as depicted in table 2 show that between public governance indicators have a strong correlation each other ($r > 0.6$, $p<0.01$).

The result indicates that public governance indicators are an integral part of public governance variable and have linearity in terms of its relationship. If the country has a high score in certain indicator of public governance, in that country will also have a high score for other public governance indicators. The most convincing correlation among public governance indicators is between rule of law and control of corruption ($r=0.953$, $p<0.01$). The second is a correlation between rule of law and government effectiveness ($r=0.944$, $p<0.01$) and the third is the correlation between regulatory quality and government effectiveness ($r=0.935$, $p<0.01$). Based on top three highest correlation magnitude between public governance indicators, it implies that the things related law and regulations are fundamental factors in order to achieve good public governance.

Hypothesis Testing

There are six hypotheses proposed in this research. All hypotheses proposed are summarized in Table 3. The hypotheses are basically predicting that good public governance practiced by the country will have a positive impact on the performance of the country in terms of its ease of doing business. Design of the research is exploratory, therefore, the hypotheses are only discovering a correlation between two independent variables. The research is not intended to reveal a causal relationship between good public governance practice on ease of doing a business performance.

Based on information depicted in Table 3, it shows that all proposed hypotheses are supported. All public governance indicators are positively and significantly associated with ease of doing a business performance.

Table 3. Summary of Hypothesis Testing

Hypothesis	Pearson Correlation Coefficient	Conclusion of Proposed Hypothesis
H1: Public accountability has positive and significant correlation with ease of doing business performance	0.606*	Supported
H2: Effectiveness government has positive and significant correlation with ease of doing business performance	0.865*	Supported
H3: Regulatory quality has positive and significant correlation with ease of doing business performance	0.881*	Supported
H4: Control of corruption has positive and significant correlation with ease of doing business performance	0.744*	Supported
H5: Rule of law has positive and significant correlation with ease of doing business performance	0.816*	Supported
H6: Political stability has positive and significant correlation with ease of doing business performance	0.584*	Supported

**. Correlation is significant at the 0.01 level (1-tailed).*

The magnitude of the correlation indicates strong correlation ($r > 0.6$) except for hypothesis 6. There is a note for correlation between political stability and ease of doing a business performance. Even though the correlation is positive and significant, however, the degree of correlation is relatively moderate ($r = 0.584$, $p<0.01$). It implies that that political stability as an indicator of public governance has no explanatory power in predicting ease of doing a business performance. However, in general, public governance indicators overall are a reliable instrument for predicting ease of doing a business performance. It is supported by statistics correlation results that all public governance attributes, except for political stability, indicate a strong correlation with ease of doing a business performance ($r > 0.6$, $p<0.01$).

The results of correlation analysis as presented in Table 3 implies that there is linearity between the practice of good public governance with ease of doing a performance. The country that has a high index score of public governance, there is a tendency to have also a high score of ease of doing a performance. It implies that if the country is consistently applied the good practice of public governance, benefits such as ease of doing business performance will be obtained by the country.

Conclusion

The findings of the research can be summarized that public governance has a positive and significant correlation with ease of doing a business performance. Overall, the magnitude of the correlation between indicators of public governance and easy of doing business performance is strong. However, the indicator of public governance namely political stability shows the moderate magnitude of correlation with ease of doing business performance.

The practice of good public governance in governmental institutions may have an impact on country's ease of doing a business performance. The foundation of ease of doing business is a commitment from government institutions to facilitates private sector organizations with the friendly business environment. Rules and regulations that are in favor of the business organization, low-cost economy, simple bureaucracy are the real output of practicing good public governance that relates to achievement easy of doing a business performance. The findings are in line with the basic of a theoretical framework that implementation of good governance principles in governmental institutions will contribute to the creation of a friendly business environment.

In order to achieve a conducive environment for starting up business among private sector organization, the government institutions must provide clean government by eradicating corruption practice in the bureaucracy. Corrupt behavior among government officials may lead to high transaction cost for the business organization. Avoidance of the potential foreign investor and withdrawal existing investors are possibilities of the impact of corrupt government institutions.

Regulatory quality provides a positive expectation for a business organization with regulations that encourage business growth through streamline bureaucracy, complicate procedures. Rule of law gives business organization confidence related legal certainty and law enforcement. Domestic political stability facilitates business organization confidence that the sustainability of business activities will not hamper by domestic political chaos. The government may be more focus on administering business organization in stable political condition. The effective government gives benefits for business organization in terms of quality of services and quickness. Lastly, public accountability gives a lesson to a business organization that they have a responsibility to stakeholders.

Suggestion for next similar research, additional the time period of investigations is necessary. İnvolving more countries with longitudinal data panel are necessary to be analyzed. İn order to get more detail information about the association between good public governance practice and ease of doing a business performance, a case study is encouraged to be conducted.

It is expected that comprehensive information about the impact of practicing good public governance on easy doing business will be revealed. This research used an explorative approach which concern about the relationship between two independent variables, therefore, upcoming research is suggested to use multiple regression analysis.

Notes on Contributor

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