Studying the Effect of Indicator quality of Governance on Income Distribution using panel Data; A Case Study of some selected countries

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Abstract

Concerning the increasing trend of income inequality and the growth of Sustainable, economic problems, Higher rates of unemployment, expansion of urbanization, economic incompetence, uneven expansion of public sectors and lack of economic justice in different societies especially in developing countries, and the role of government in carrying out their duties to achieve a better distribution of income being highlighted, the need for good governance is strongly felt. Accordingly the main objective behind the present research was to study the effect of Indicator quality of Governance on income distribution for selected countries regarding the Organization of Islamic Cooperation member (OIC) and countries of the Organization for Economic Co-Operation and Development (OECD), using panel data and Sen adjusted social welfare function during 1999-2010 was used and estimated through Evievs8 Software. The results showed that the quality of governance indicator had a significant impact on reducing the inequalities in the two groups, but the coefficient for OECD countries was less than the one for OIC member countries and it could only lead to improvement of the economic situation, boosting economic growth and reducing income inequality only if the policies of good governance were implementation. The reasons were several involving lack of appropriate policies, corruption and in efficient be accuracy.

Introduction

Since the advent of reflection on development as a global concern after World War II, one of the goals of development has always been achieving better living standards, improving social welfare, and considering the importance of development in improving the human's life. In this status quo, one of the Challenges of development custodians has been the pertinent role of Governments. In different periods, the key to the puzzle of Development is summarized in the maximum, minimum and good governance: first period has begun with the end of World War II and continues by the late 1970s and continues to early 1990s, the minimum government pattern. Many of these Problems formed a post-Washington consensus.

In a post-Washington consensus for a new criterion egalitarians development, sustainable evaluation of the government is propounded as good Governance. Within good governance, the main emphasis is on the relationship between government and People. Considering the condition of developing countries this is largely considered that what is concerned is not quantity, but the quality of services provided by the Government, that the paradigm of Good governance with market and civil society as two other pillars of the community at the same time play the role of moderator towards each other (Komeyjani and Salatin, 2009). Given that the major

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problems inside transition countries is unequal distribution of income and low economic growth, and the results of theoretical and experimental studies have been conducted in these countries, including African and Latin American countries in recent years which had set its target growth, indicating that economic growth is not necessarily accompanied with reduction in inequality, and despite their comparative success in economic growth, the situation does not improve [6].

With regards to this matter, the importance of income distribution is to the extent that almost all economists cited income distribution as one of the main goals and tasks of the government that can be considered a clear and specific task for an efficient government, which allows the quality of services provided by the government, and is caused through appropriate interaction between three society institutions, government and private sector, which is one of the factors of good governance. With regards to the importance of income distribution on economic growth in countries, so the main objective of this research was to study the effect of indicators of good governance on income distribution for selected countries, Organization of Islamic Cooperation member countries of OECD countries using panel data, and Sen adjusted social welfare function during 1999-2010 [6].

In this Context, this paper has been developed in five sections. Within the second part the theoretical and Research literature in the field of good governance and income distribution is examined. The second part describes the theoretical foundations and specified models are specified. The fourth section deals with the analysis of the research model and the final section is a conclusion of model and policy recommendations.

Theoretical Foundations:
Definition of good governance:

World Bank and IMF urged the governments of developing countries to reform the policy as a condition of accepting credit from the early and mid-1980s respectively. This new approach, which was introduced under the structural adjustment policies, was widely agreed on by Washington policy circles such as the World Bank, the IMF, the Treasury and the Federal Reserve America. In mid-1990s, adjustment policies and institutional economists such as Kaufmann, et al., [5] were widely criticized. His critical comments in the form of consensus politics Post-Washington Consensus were introduced in 1998. The Post-Washington Consensus, government and market institutions are complementary rather than competing institutions. Therefore, the discussion of intervention or non-intervention should be replaced with the efficiency and effectiveness of government intervention. Successful provision of these institutions is often introduced as good governance. The World Bank defines governance as the traditions and institutions by which authority in a country is applied to the common good. The parameters of the World Bank are: 1- voice and accountability 2- political stability 3- government effectiveness 4- quality of laws and regulations 5- the rule of law and 6- control of corruption [7].

Background of the study:

Safique and Haq, [12] in an article examined the impact of good governance indicators on income distribution and economic growth for SAARC countries between 1996-2005. They testified the influence of public policy (good governance) on two variables of economic growth and income distribution through the Sen welfare index application using Gini coefficient variable as a measure for income inequality. The results showed that the role of good governance indicators influences on income inequality, and subsequent reduction in inequality within those countries. Akram et al., [1] examined the effect of Long-term and short-term relationship between poverty governance and income inequality on poverty in Pakistan through autoregressive distributive lags (ARDL). During 2008 period, the results of this study indicated positive correlation between poverty and inequality in both short and the long run. Gyimah-Brempong [3] examined corruption, economic Growth, and economic inequality in Africa. Their results signified that corruption increase has a positive relationship with income inequality.

Many extend studies have been done about good governance, income distribution, and income inequality, indicators affected by some other factors and the effect of these indicators on economic variables; to name some, we can mark some out as: Introduction to the Theory of Good Governance [8], the impact of good governance and economic growth in selected countries, OPEC and OECD [6,7] Effect of quality of governance and economic growth in Iran and selected countries neighbors (Turkey and Pakistan) [6] in which the impact of good governance measures as been analyzed on the human development index of south East Asian Nations [13] the role of good governance in improving the functioning of government spending [11] the rule good to attract foreign direct investment in Iran [10] evaluation of good governance from the perspective of Islam and its impact one economic growth [9] etc., but overall detailed study on the impact of good governance on the distribution income has not yet been performed.

The present study compared to the other articles mentioned, as well as existing research in this area, has differences in the types of indicators used with some examples of the studied countries in a way that unlike the social welfare functions in which the welfare function of private goods consumption has not been much considered while it's good to know the impact of social welfare institutions and governance policies. In fact, the institutions will have a profound impact on economic performance. Here, it's good to note the role of
Governments in preparing for the outstanding economic growth and development, and market failures that the governments can provide the public goods and services and other policies, to improve the status of social welfare officials. Accordingly, in the social welfare function, in addition to the consumption of private goods, we have entered public goods which we believe can lead to failure status in government.

Data Analysis: Specifying The Model:

Data Sources:
In order to testify the theoretical foundations of the purposes outlined in the past section, Time Series data related to the three countries were mapped over 2010-1999. The selected template has been used for the following countries for 3 groups in order to allow the continuation of quality and the impact of different conditions on the distribution of income provided by the model. The first group included 48 members of Organization of Islamic Cooperation and the second group consisted of 30 members of the OECD.

Procedures:
The method used in this research was analytical-descriptive, and also in order to reconcile theory with the realities, we examined the relationship between variables using statistics and numbers, and after reconciling with theories, we examined introduced assumptions in order to judge rejecting or accepting the introduced assumptions. In gathering the data and information, librarian method was used. WDI (2014), WGI statistics and United Nations development Programs have been used for estimation purposes.

Model specification:
According to various influential variables on the distribution of income, for the relationship between the quality of governance on the distribution of income in two groups of selected countries in the above mentioned Sen adjusted social welfare function Can be used as follows.

\[
Gini_{it} = \alpha_i + \beta_1 Gqi_{it} + \beta_2 I_{it} + \beta_3 G_{it} + \beta_4 Cons_{it} + \rho_5 UPI_{it} + \rho_6 Eii_{it} + \rho_7 Demo_{it} + \epsilon_{it}
\]  

Where (i) denotes the observed cross sections or units, (t) represents time, ( )and( )are the coefficients related to the effects of the cross respectively.

Gini: Gini coefficient as a measure of the inequality index was used as the dependent variable. Gqi is good governance and the quality of the candidates adapted from Gani and Duncan's study (2004) based on the arithmetic mean of 6 indicators of good governance. I is the investment spending per capita private sector in constant prices of 2005, when the variable gross fixed capital formation per capita in constant prices of 2005 as an alternative measure. G ratio is the General government expenditure to GDP per capita in constant 2005 prices, Cons is the expenses final consumer per capita in constant prices 2005. The three control variables in the model were the UP rate of urbanization, Eii economic freedom index data from the Institute; taken from Freedom House and Demo of democracy from the Institute of information rankings democracy. "U" also can be taken as an error.

Model Analysis:
Unit root test in integrated models:

Econometric models in empirical works are based on variables of stationary assumptions. Stationary method is utilized to avoid spurious regressions and to find a balanced relation between variables [14]. So before using these data, we should be assured of their status as being Stationary or not. In this section, for unit root test of Levin, Lin and Chu test and In Pesaran Shin test was used. The results have been depicted in table 2, which is done by Eviews Software. The first model is for the OIC member countries and the second model depicts the OECD countries.

<table>
<thead>
<tr>
<th>Second Model</th>
<th>First Model</th>
<th>Name of Variable</th>
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<tbody>
<tr>
<td>IPS</td>
<td>LLC</td>
<td>IPS</td>
</tr>
<tr>
<td>-5.84</td>
<td>-6.82</td>
<td>-2.19</td>
</tr>
<tr>
<td>-5.99</td>
<td>-6.10</td>
<td>-5.54</td>
</tr>
<tr>
<td>-2.54</td>
<td>-6.64</td>
<td>-2.52</td>
</tr>
<tr>
<td>-3.11</td>
<td>-4.26</td>
<td>-3.34</td>
</tr>
<tr>
<td>-2.42</td>
<td>-5.02</td>
<td>-2.23</td>
</tr>
<tr>
<td>-3.82</td>
<td>-4.71</td>
<td>-14.21</td>
</tr>
<tr>
<td>-2.69</td>
<td>-4.18</td>
<td>-2.19</td>
</tr>
<tr>
<td>-4.67</td>
<td>-4.56</td>
<td>-6.08</td>
</tr>
</tbody>
</table>

Source: Researcher findings
It is observed that all variables of the model in 5% confidence interval are in Stationary level. This means that all variable stationary.

**Diagnostic tests in the integrated model:**

The use of pooled data from two test patterns is important. Homogeneity test sections must be done. If the assumption $H_0$ that based on the homogeneity of the cross section is rejected, second test namely Haussmann test for investigating random effects versus fixed effects should be used. The results of the test stipulated in above equations represented below.

Concerning the information of models, the results of F test and Hausman test for both models are as follows:

<table>
<thead>
<tr>
<th>Table 2: The results of F test</th>
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<tbody>
<tr>
<td>Test</td>
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<tr>
<td>F test</td>
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<tr>
<td>Hausman test</td>
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</tbody>
</table>

Source: results of researcher

In the first model $F=104.56$ (Limer Statistics) shows that different sections have significant differences, so the fixed effect is not rejected. In other words, Pooled Regression is rejected. Also in the second model $F=62.1$ shows a significant difference between different sections, so the fixed effect is not rejected. In other word, Pooled Regression is rejected. So the panel data is selected for estimating the data. Also, the results of Haussman test for determining the Method of random or fixed Effects show that also the Hausman test for the two groups shows that the model with random effects versus model with fixed effects is not supported. Accordingly, this is an optimum method for estimating the model with fixed effects.

**The Estimation Results For The Two Groups of Countries In The Specified Models:**

**The member states of the organization of Islamic cooperation:**

The results of estimating equation in logarithmic form for the OIC member states areas follows:

$$
\log(Gini) = 3.08 - 0.059\log(gqi) + 0.004\log(cons) - 0.009\log(I) + 0.068\log(G)
+ 0.067\log(U) - 0.15\log(Ei) - 0.16\log(Demo)
$$

$$
R^2 = 0.983 \quad F = 324.367 \quad D.W = 1.99
$$

**OECD countries:**

The results of estimating equation in logarithmic form for OECD countries areas follows:

$$
\log(Gini) = 4.48 - 0.016\log(gqi) - 0.147\log(cons) - 0.03\log(I) + 0.042\log(G)
+ 0.153\log(U) - 0.142\log(Ei) - 0.279\log(Demo)
$$

$$
R^2 = 0.982 \quad F = 298.85 \quad D.W = 2.04
$$

The results of the estimation of the models indicate that in both groups the quality of governance index significance have a negative impact on the Gini coefficient, also the rate of this coefficient in OECD countries is less than the one for OIC member countries and due to several reasons including lack of appropriate policies, corruption, inefficient bureaucracy which if the policies of good governance is implementation, it can lead to improvement of the economic situation, boost economic growth and income inequality is reduced.

Final consumption expenditure per capita in OIC member countries had appositive impact while in OECD countries it had a negative impact on the Gini coefficient, but it is significant only in only in the OIC countries. Private sector investment spending, had a negative impact for both groups, but only in OECD countries it was significant. Public sector expenditure to GDP per capita for the OIC member countries and the OECD positive was not significant for both groups. Urbanization rate in the three groups had a positive impact on the Gini coefficient, but it was not significant. The index of economic freedom and democracy in both groups was significant and had negative impact on the Gini coefficient. The results show that the degree of economic freedom in OIC member countries is lower than in OECD countries. The absence of a clear vision for investment, capital market weakness, lack of property rights so foreign investment, much of the bureaucracy, the multiplicity of tariff, non-independence of the judiciary, state and lack of clear property rights has led the degrees of freedom economic to decline compared with the OECD countries.

**Conclusion and policy Recommendations:**

The present study was aimed to investigate the effect of governance equality on income distribution of the OIC member countries and OECD countries over the period 2010-1999. Using panel data for fixed effects and
the modified based social welfare of [12] According to the results, the policy recommendations are offer hitherto:

1. Due to significant negative impact on the quality of governance and the Gini coefficient for these countries, it is recommended that they should have policy package for the achievement of better governance model for the implementation of economic reforms, judicial, administrative, managerial and policy improvement and development of civil society.

2. Due to the negative impact of democracy on income inequality it can be expressed as more democracy stimulate poor income distribution it may strengthen the Commonwealth and more efforts should be targeted to wards groups and they be able manage new issues in the current world.

3. Due to the negative impact of economic freedom index on the Gini coefficient it is recommended that adjustment policies be done if that is not the point and discrete. Otherwise, fast and detrimental effects on the structure of income distribution and poverty can be in order. Gradually adaptation to the economic, social and cultural feasibility native to the implementation of these policies is required as initial steps in the reduction of inequality and social welfare.

REFERENCES