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Does institutional quality matter in fostering social progress: A cross national examination

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A B S T R A C T

The first Social Progress Index (SPI) report was released in 2013; a handful of studies examined the determinants of social progress at country level as an instrument in evaluating nation's prosperity. This study focuses on determining the relationship between institutional quality measured by the World Governance Index (WGI) and social progress measured (SPI).The results are based on the secondary data from 107 countries over a four year period (2014-2017), after controlling Gross Domestic Product per capita, innovativeness and trustworthiness. The result was in favor of the fixed effect model. The findings illustrate that institutional quality was consistently significant in fostering social progress. This study is unique in that, it is the first that examined the role of formal institutional quality in promoting social progress at country level by using SPI as a measurement of social progress.

1. Introduction

Welfare, quality of life, happiness and wellbeing at country level are indicators used to measure a nation's prosperity as oppose to Gross domestic product (GDP) (Osberg, 2001). Traditionally Gross Domestic Product (GDP) has been utilized as an economic indicator in the context of social progress. GDP was considered the most effective method to measure the progress of a nation's prosperity, and its development (Herrmann, 2012). Nonetheless, many academics posit the need to move away from economic growth indicators and prioritize equity and wellbeing. The GDP cannot be considered as a tool for assessing the performance of nations in the context of serving citizens (Osberg, 2001; Greve, 2017), as it focuses only on monetary aspects and excludes the social and environmental priorities of citizens lives (Fleurbaey, 2009). Furthermore, politicians have also recognized that GDP is no longer a sufficient tool in assessing societal progress as it was not originally developed to capture the social facet of development. For example in 2008, the French President Nicolas Sarkozy commissioned Joseph E. Stiglitz to chair a commission on the Measurement of Economic Performance and Social Progress (Yee & Chang, 2011). The report conclusively determined that for governments to comprehend the performance of the economy and society, comprehensive indicators were needed to accurately assess wellbeing. Social Progress is one of the modern concepts considered as a prosperity indicator that can fill the GDP deficiency,

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as a wellbeing and environmental indicator. Social progress is defined as "the capacity of society to meet the basic human needs of its citizens, establish the building blocks that allow and create the conditions for all individuals to reach their potential" (Social Progress Imperative, 2018).

Countries have unique conditions, characteristics and features that may play an important role in many aspects of its prosperity. Prosperity can be classified economically and socially. In the context of economic development, institutions can be classified as formal and informal institutions (North 2006), they are considered crucial if they are defined as good or efficient institutions, which is based on the outcome quality measured by governance in six areas (voice and accountability, control of corruption, government effectiveness, political stability, rule of law and regulatory quality). Institutions proved it's effective role in the area of foreign direct investment (Bailey, 2018; Bouchoucha & Benammou, 2018), entrepreneurship (Aparicio et al., 2016), and economic development (Knack & Keefer, 1995). Furthermore, good institutions can contribute to the social needs of citizens and societal progress. In the context of social development, the relationship between institutional quality and social development on society has been examined in the context of wellbeing (Bjørnskov et al., 2010; Helliwell & Huang, 2008), quality of life (Nikolova, 2016), and national happiness (Ott, 2010; Ott, 2011; Rode, 2013). As it is not enough to improve the monetary side of citizens lives, policymakers in developed countries have a clear understanding of the importance of institutions in enhancing the output of their policies, which is evident in the findings of the SPI (2013-2018) over a six year period. Since the first edition of (SPI) in 2013, most of the attention has been given to measure this type of development, although little attention or empirical research in the area of the determinants has been conducted.

Grounded in transaction cost theory and intuitional theory, we assume that institutions, through adopting good governance, will improve the economic development and act as a motive for policy makers to manage and invest rationally to improve citizens conditions and their progress in both aspects of development (economic and social). Furthermore institutional theory holds the view that institutions drive and shape the behavior of firms and individuals (Alsaad et al., 2018).

The main purpose of this study was to examine the impact of institutional quality in enhancing social progress through examining if a country's governance has a role in fostering its social progress position. To analyze the relationship between institutional factors and social progress at country level, a panel data method was utilized for 107 countries over four years from 2014 to 2017. This study contributes in different ways: firstly, according to our knowledge this study is unique in that it is the first that examined the role of formal institutional quality in promoting social progress at country level by using (SPI) as a measurement of social progress. Secondly, the research was comprised of a large amount of data; consisting of 107 nations. Thirdly, the research employed principle component analysis (PCA) to summarize the shared variation of governance indices into one synthesis variable. Finally two types of controlling variables (economic factors consisted of GDP per capita and, social control variables represented by trustworthiness and innovativeness) were used.

This paper is structured into four sections. Firstly it introduces the concept of social progress, institutions and institutional quality proxied by the World Governance Index. Secondly the research will describe the data and methodology used. Finally the results and findings are discussed with relevant conclusions made, research limitations and future research recommendations proposed.

2. Literature Review

2.1 Social Progress

Social progress as defined by the Social Progress Imperative 2018 is "the capacity of society to meet the basic human needs of citizens, establish the building blocks that allow and create the conditions for all individuals to reach their potential". In the same vein Este (1984) stated that the adequacy of social provision "refers to the changing capacity of governments to provide for the basic social, material, and other

needs of the people living within their borders for food, clothing, shelter, and access to at least basic health, education, and social services". Citizen needs are recognized not only as material needs but as social needs as well (Estes & Morgan 1976). In relation to these needs, previous studies confirmed the deficiency of gross domestic product (GDP) as a tool to measure it (Osberg, 2001; Greve, 2016).

The measurement of these needs using GDP is limited in scope and not comprehensive (Bečić et al., 2012) and is not considered a valuable tool in measuring social progress and society's wellbeing (Greve, 2016; Decancq & Schokkaert, 2016). Although GDP deficiencies are evident it can still play an important role in assisting governments serve their citizens, as GDP is a tool used in assessing citizens quality of life (Sen, 1999; Agarwal & Samanta, 2006). The Social Progress Report (2017) shows that the relationship between GDP and social progress is bidirectional which means that the outcomes of social progress works as essential conditions for more productivity and, without good economic performance governments lack the capacity to invest in health, education and technology, thus indicating an interdependent relationship. On the other hand, there is no correlation between economic growth and social progress (Agarwal & Samanta, 2006). To explain this contradiction we use the classifiction of policy makers of Bruno and Faggini (2017) which classified policymakers into two types: selfish policy makers and unselfish policy makers. This classification reflects the relationship between economic growth and social progress and illustrates that a positive relationship exists in relation to unselfish policy makers only.

2.2 Social progress measurement

Some studies used other indices as indicators to measure social progress such as sustainable development indicators (Bečić et al., 2012). One initiative by Agarwal and Samanta (2006) produced an index for social progress based on aggregate indicators including poverty, hunger, primary education and gender quality in education, which was based on data from the Millennium Development Goals (MDGs). In this context Decancq and Schokkaert (2016) tried to measure the wellbeing which is one aspect of social progress through equivalent incomes. The Social Progress Index has not been the first attempt in measuring nation's development, as there were other initiatives, for example the Human Development Index, National Welfare Index, and the National Wellbeing Index. These data research tools have a strong relation and correlation to each other as all are willing to measure the progress beyond GDP (Decancq & Schokkaert 2016; Greve, 2016).

The Social Progress Index (SPI) is the newest tool that measures a nation's progress through analyzing three main areas of an individual's life: 1. basic human needs, 2. foundation of wellbeing, 3. opportunity. SPI distinguishes itself by measuring the output not input; it is not dependent on proxy but rather direct and actionable measurements. In order to achieve these points as mentioned the index covers three main dimensions are incorporated into 12 components (Table 1), with principal components analysis applied for determining each indicator's weight. The index categorizes countries into six tiers: very high social progress, high social progress, upper middle social progress, lower middle social progress, low social progress and very low social progress (Table 3). In the Social Progress Index, hierarchical clustering methods are used to classify the countries into tiers, thus SPI does not set arbitrary weights.

Table 1
Social Progress Index component-level framework

Basic Human Needs	Foundation of wellbeing	Opportunity
• Nutrition and basic medical health • Water and sanitation • Shelter • Personal safety	• Access to basic knowledge • Access to information and communication • Health and wellness • Environmental quality	• Personal right • Personal freedom • Inclusiveness • Access to advanced education

2.3 Overview of countries position in (SPI)

The importance of social aspects has concerned policymakers in most countries. Following the report from the Social Progress Imperative 2017, Denmark and Norway were ranked number one in 2017, countries such as Nepal, Côte d'Ivoire, Kyrgyzstan, Togo, Bangladesh, Sierra Leone and Ghana succeeded in improving their positions by 3-4 points. Some countries scored high in income but were still considered under performers in social progress compared with other countries that have high income such as France, United States, Kuwait and Saudi Arabia, in comparison to other countries that have high income and considered over performers in social progress, for example Chile, New Zealand, Portugal and Uruguay. It is evident that some countries worked hard to keep their positions or improved, even though they are considered less developed and have lower incomes such as Chile and Uruguay. We believe that improving social progress and utilizing it as a tool can aid in building and maintaining a country's image and brand, and policy makers' image as well.

2.3 Institutional Quality

According to North (1991), institutions are "the rule of the game in society". According to Rodrigguez (2013) "defining institutions is notoriously difficult and the current literature on the topic does not agree on a common definition", however, institutions could be classified into two types: 1. Formal institutions 2. Informal institutions. To differentiate between the two types, formal institutions have short term change while informal that depicts a belief system, social norms and cognitive aspects requires more time to change (North, 2005). Therefore Rodrigguez (2013) emphasized that "bringing institutions into the development process is easier said than done".

Rodrigguez (2013) summarized the main problems in the institutional literature. Firstly, there is no clear definition of efficient institutions, secondly the difficulties related to the measurement based on space and time. Finally, building up the right combination of formal and informal institutions can prove complex. However, previous studies tried to overcome these issues by considering governance as an indicator for efficient institutions or good institutions.

"Governance is the exercise of political, economic and administrative authority necessary to manage a nation's affairs" (OCED, 2006), thus institutions are responsible for managing societal issues. According to North (1991, 2006) institutions are the creators of how individuals interact in society. The development of societies economically and socially is linked to governance, with governments adopting good quality governance in its design and in formulating and implementing appropriate policies (Quibria, 2006). Previous studies confirmed the importance of institutional quality in attracting foreign direct investment, increasing human development, promoting entrepreneurship and enforcing corporate social responsibility (Bailey, 2017; Kurual, 2017; Balcerzk, 2017; Aparicio, 2016; Ioannaon & Serafeim 2012; Jackson & Apostolakou 2010, Lim & Tsutsui 2012). Moreover scholars examined the effect of institutions on nations wellbeing which is considered one dimension of social progress (Helliwell et al., 2018). Building on the overlap between social progress and other indices measuring the progress of wellbeing, quality of life and environmental progress, this study will examine the role of institutional quality in the development of social progress by framing it in the context of intuitional theory and transaction cost theory.

3. Empirical Methodology and Data

3.1 Data

This study examined the effect of institutional quality on social progress. To examine the relationship, we utilize a large panel data set involving 107 countries over four years including 2014 through 2017. Institutional quality proxied by governance index while the dependent variable proxied by SPI and three control variables (GDP per capita (PPP), innovativeness and trustworthiness).

Table 2
Variable and data sources

Variable	Measurement	Source
Independent variable :		
Institutional quality	Governance indices	World Bank- Governance indicators
Dependent Variable :		
Social progress	Social progress index	Social Progress Imperative
Control Variables :		
Economic factors :		
Economic development	GDP per capita (PPP)	World Bank's WDI
Social factors :		
Innovativeness	Global innovation index	World Bank's WDI
Trustworthiness	Global Competitiveness index	World Economic Forum

Table 3
Countries included in the study organized into the tiers of SPI (2017)

Very high social progress	High social progress	Upper middle social progress	Lower middle social progress	Low social progress	Very low social progress
Denmark	Belgium	Mauritius	Lebanon	Kenya Bangladesh Cambodia	Chad
Finland	Spain , Japan	Panama , Bulgaria	Moldova	Rwanda	
Iceland Norway	United States	Brazil ,Romania	Sri Lanka Kazakhstan	Lesotho	
Switzerland Canada Netherlands	France ,Portugal	Serbia , Peru	Algeria	Pakistan	
Sweden	Slovenia	Mexico ,Colombia	Azerbaijan Kyrgyzstan Morocco	Tanzania	
Australia	Czech Republic	Malaysia, Tunisia	Indonesia Botswana	Zimbabwe	
New Zealand	Estonia	Albania , Georgia	Nicaragua	Nigeria	
Ireland	Italy , Chile	Montenegro	Egypt ,China	Uganda Cameroon	
United Kingdom	Korea, Republic	Jordan	Mongolia	Mali	
Germany	Cyprus	Saudi Arabia Armenia	Iran	Ethiopia	
Austria	Costa Rica	,Paraguay	Honduras		
	Israel ,Slovakia	Turkey ,Thailand	Ghana ,Nepal		
	Uruguay	Dominican Republic	Tajikistan		
	Poland ,Greece	Ukraine	India ,Senegal		
	Latvia , Lithuania	South Africa			
	Croatia	Russia			
	Hungary Argentina	Philippines			
		Bolivia			

3.2 Methodology

As mentioned above this study covers data over four years relating to 107 countries. Cross-national panel data set is advantageous to inspect societal changes and impacts. Socialists maintained that social changes do not occur immediately but rather they need a period of time to materialize and be observed in a society (Meyer, 2010). In this sense, the determinants of social progress across countries should be longitudinally assessed (Alonso-martínez, 2018). Keeping this in mind, this research endeavor constructs a time-lagged dataset through which the impact of past governance levels and other covariates on future levels of social progress could be assessed over time. Precisely, we used governance indicators and other covariates values from 2013 through 2017 to predict social progress levels from 2014 to 2017. While time-lagged dataset is advantageous in addressing variation over time, it also controls for potential sources of endogeneity. We estimated the following equation Eq. (1):

$$SOCIALPROGRESS_{i,\,t} = \alpha_i + Z_i + X_{i,t-1} + GOVERNANCE_{,t-1} + u_{i,t-1,} \quad (1)$$

where $SOCIALPROGRESS_{i,t}$ is the social progress in country i in year t, Z_i is a vector of observed and unobserved time-invariant variables of country i, $X_{i,t-1}$ is a vector of time-variant variables of country i in year $t-1$, $GOVERNANCE_{i,t-1}$ is the quality of governance in country i in year $t-1$, and $u_{i,t-1}$ is the error term. The explanatory variables in Eq. (1) include quality of governance, besides other controls. To measure governance quality, this research uses the governance indicators, composed of the Governance Indicators (WGI) project (Kaufmann et al., 2011). According to WGI, the quality of governance is assessed by aggregate indicators of six broad dimensions of governance which include 1) Voice and Accountability, 2) Political Stability and Absence of Violence/Terrorism, 3) Government Effectiveness, 4) Regulatory Quality, 5) Rule of Law, and 6) Control of Corruption. These indicators are aggregated and summarized from a large data set collected from multiple well-established sources. The data regarding these indicators have been reported annually by the WGI since 1996. However, while governance indicators are widely used in the literature, recent investigations reveal that the governance indicators are highly collinear and essentially measure the same broad concept (Knoll & Zloczysti, 2012; Langbein & Knack, 2010). Therefore, instead of considering all of the governance indicators in our model, we perform a principal component analysis (PCA) in order to summarize the shared variation of these indicators into one synthetic variable representing the quality of governance. The result of PCA indicates that only the first component has eigenvalue above 1. Moreover, the first component accounts for 85.8% of the variance in governance indicators (see Table 4 Table 5 and Fig. l). Accordingly, we use the resulting first component for further analysis.

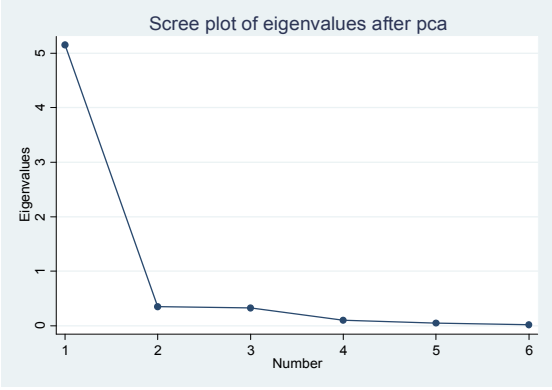

Fig. 1. Screen plot of eigenvalues

Table 4
Eigenvalues of the correlation matrix

Component	Eigenvalue	Difference	Proportion	Cumulative
Comp1	5.15147	4.79981	0.8586	0.8586
Comp2	0.351652	0.02574	0.0586	0.9172
Comp3	0.325911	0.223327	0.0543	0.9715
Comp4	0.102584	0.05468	0.0171	0.9886
Comp5	0.047904	0.02742	0.008	0.9966
Comp6	0.020484	.	0.0034	1

Table 5
Factor pattern on the first component

Variable |	Comp 1
Voice and Accountability	0.3701
Political Stability and Absence of Violence	0.3733
Government Effectiveness	0.423
Regulatory Quality	0.4236
Rule of Law	0.4324
Control of Corruption	0.4224

With regard to vector $X_{i,t-1}$ of time-varying variables in Eq. (1), we include some control variables in order to minimize the bias of omission salient predictors. Our revision of prior research reveals that there are limited candidate control variables to include in our model due to the scant research on cross-national social progress. A highly recommended control variable is (the log of) GDP per capita, symbolized by *Log(GDP* $_{i,t-1}$*)*. GDP per capita is a versatile control variable because economic growth, as measured by GDP, offers more resources to invest in social-related issues. Moreover, GDP is highly correlated with several other time-varying variables that may influence social progress. Prior research shows that GDP per capita is a silent predictor of many societal phenomena (Easterlin, 1995; Bjørnskov et al., 2010). Accordingly, we control for the effect of GDP per capita. The GDP per capita values were obtained from the World Bank data bank.

In accordance with Alonso-Martínez (2018), we also control for the effect of innovativeness as measured by the Global Innovativeness Index, denoted by *INNOVATIVENESS* $_{i,t-1}$. Alonso-Martínez (2018) found that innovativeness contributes significantly to social progress and development. The data of this control variable was obtained from the Global Innovativeness Index, composed by the World Economic Forum (2018). Additionally, we control for the effect of social capital measured by trustworthiness and confidence index denoted by *TRUSTWORTHNESS* in our regression, trustworthiness was used in previous studies as an indicator to trust and honesty (Alsaad et al., 2017; Bjørnskov et al., 2010). The data of this control variable was obtained from the Global Innovativeness Index, composed by the World Economic Forum (2018).

The descriptive statistics of all covariates are shown in Table 4. Notable is that there is a high correlation between *GOVERNANCE* and *INNOVATIVENESS* (r=0.87). To examine whether multicollinearity would bias our results, we estimate the variance inflation factors (VIFs). The result reveals that none of the VIFs was above the threshold of 5, suggesting that multicollinearity is not an issue in this study. Moreover, we have evaluated the assumptions of normality and heteroscedasticity. Both skewness and kurtosis tests have indicated that the data we use does not depart from normality. White's test for heteroscedasticity also provides support for constant variance.

Table 6
Descriptive statistics

Variable Name	Mean	Std. Err.	(1)	(2)	(3)	(4)	(5)
SOCIALPROGRESS (1)	70.87	0.68	1.00				
TRUSTWORTHNESS (2)	4.52	0.04	0.38	1.00			
INNOVATIVENESS (3)	39.32	0.58	0.86	0.48	1.00		
GDP (4)	24177.17	1088.03	0.89	0.38	0.79	1.00	
GOVERNANCE (5)	0.14	0.12	0.88	0.55	0.87	0.79	1.00

3.3 Empirical Results

Hausman test was utilized to determine the appropriate panel analysis technique. The result of this test indicates that the fixed effect model was appropriate for this study as compared with the random-effect model. To assess the true impact and rule out alternative explanations of the effect of *GOVERNANCE*, four models were estimated (Model 1, 2, 3 and 4). In model 1, *GOVERNANCE* is regressed alone against *SOCIALPROGRESS.* Along with *GOVERNANCE*, gradually *Log(GDP) and TRUSTWORTHNESS*, *INNOVATIVENESS* were added into model 2, 3 and 4, respectively.

The estimation of Eq. (1) is provided in Table 7. The estimation reveals that *GOVERNANCE* is consistently significant in the three models (1, 2, 3 and 4) at significance level 0.01, suggesting that the slope estimate of *GOVERNANCE* is robust to the insertion of the three time-variant control variables, *Log(GDP), TRUSTWORTHNESS* and *INNOVATIVENESS*. Similarly, *Log (GDP)* always provides a significant predictor of social progress, except in model 2. Surprisingly, both *INNOVATIVENESS and TRUSTWORTHNESS* do not seem to influence social progress at all.

Table 7
The estimation results

Covariates	Model (1) **Coefficient (SE)**	Model (2) **Coefficient (SE)**	Model (3) **Coefficient (SE)**	Model (4) **Coefficient (SE)**	Model (5) **Coefficient (SE)**
GOVERNANCE	1.130*** (0.257)	1.093*** (257)	1.11*** (0.26)	1.18*** (0.263)	2.72*** (0.68)
GDP		1.706 (1.05)	1.77* (1.06)	2.28* (1.22)	3.14** (1.36)
TRUSTWORTHNESS			-0.22 (0.16)	-0.26 (0.16)	-.241 (0.182)
INNOVATIVENESS				-0.003 (0.01)	-.008 (0.13)
_cons	69.23*** (0.04)	52.92*** (10.07)	53.32*** (5.11)	49.70*** (11.71)	41.32*** (13.14)
R-square	0.551	0.556	0.559	0.570	0.454

Year dummy variables have been included in the regression but not reported in the model; standard errors are in parentheses. VIF values were less than 5. Significant level: *p < .01. **p < .05. *** p <0.01

To check the robustness of our results, we have examined the extent to which our results might be biased by potential endogeneity problems. We have utilized the two-stage least squares (2SLS) for this purpose. In 2SLS, instrumental variables were used to substitute for the explanatory variables that were expected to be correlated with the error term. A proper instrument is suggested to be highly correlated with the substituted explanatory variable while uncorrelated with the error term (Wooldridge, 2010). In this study, we have used the lagged value of *GOVERNANCE* and *INNOVATIVENESS* as instrumental variables. The estimation of 2SLS as shown in model (5) has indicated that the results were comparable with earlier results (model 4), providing evidence for robust results with little concern of endogeneity in the research model.

4. Discussion and Conclusions

Welfare, good quality of life, a good environment and individual wellbeing should be the most important concerns of decision-makers, as economic performance is no longer sufficient (Bruno & Faggini, 2017). This study has investigated the impact of institutional quality measured by governance on improving citizen lives, represented by social progress as a tool to measure the outcomes of country formal institutions. To our knowledge, it is the first study that examined the effect of institutional quality as a determinant for the development of a nation's social progress measured by SPI. In our sample of 107 countries we have performed a principal component analysis (PCA) in order to summarize the shared variation of these indicators into one synthetic variable representing the quality of governance. The results of PCA have indicated that only the first component had eigenvalue above 1. Moreover, the first component accounts for 85.8% of the variance in governance indicators. Hausman test was applied to determine the appropriate panel analysis technique. The results of this test have indicated that the fixed effect model was appropriate for this study as compared with the random-effect model. The result has indicated that countries with high quality institutions in terms of governance can assist in motivating to build a better position in terms of social progress. In respect of control variables, *Log (GDP)* is always a significant predictor of social progress, except in one model, however, the effect of innovativeness and trustworthiness do not seem to influence social progress at all. These results diverge and contradict previous studies but are in line with Alonso-Martínez's (2018) research. Consistent with the previous study of Agarwal and Samanta (2006), governance is highly correlated with social progress. This result corresponds to Greve (2016) as it emphasized the relationship between public policy and happiness thus overlapping with social progress in some indicators. Moreover, a number of studies have found a significant positive impact between quality of formal institutions and national happiness (Bjørnskov et al., 2010; Helliwell et al., 2018). Additionally, this significant relationship is confirmed in the context of national wellbeing which is one of the main dimensions in the Social Progress Index (Helliwell et al., 2014). In sum, in line with the importance of satisfying citizens' needs and improving their standard of living, social progress is a method of response that can be used by governments and policymakers through developing not only

economic indicators but also social and environmental indicators. To achieve this goal, institutions should be utilized efficiently through good governance.

5. Limitations

Similar to other research, this study has at least three limitations. This study used the overall score of the SPI, future studies can examine the effect of institutional quality on the social progress dimensions (basic human needs, foundation of wellbeing and opportunity). Future research may additionally study the impact of informal institutions (cultures, beliefs and social norms) (Alsaad, 2018). Finally, researchers can utilize the SPI tier classification to examine the role of institutional quality on countries in each tier. In regards to managerial implications, based on the bidirectional relationship between economic development and social progress and the theoretical framework for institutional theory and transaction cost theory, policymakers should understand that quality institutions is one method to foster this relationship by considering governance which is key to efficient institutions. This is turn, can reduce the transactional cost and improve economic development which leads to better social progress and vice versa.

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