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INSTITUTIONS: A NON-QUANTITATIVE EXPLICATION

ABSTRACT

In this paper, the meaning and nature of institutions in the economic literature are examined critically with a particular interest on its relevance to the development process of Nigeria. It suggests that the uncritical use of institution-based definitions and context-based concepts mainly from the Western world may not adequately reflect the history, socio-economic, political and cultural context in which institutions develop in Nigeria. The study, therefore, highlights the need for context-specific meaning of institutions, which takes into account the peculiar nature and problem of the Nigerian economy. It also looks at the key typologies and categorisations of institutions, the indicators widely used for judging institutional quality and the conceptual difference between institutions and organisations. The paper does so by introducing these distinctions, which help to grant a more nuanced view of the interaction between formal rules, informal norms, governance arrangements, and institutional structures in creating institutional effectiveness and development outcomes in Nigeria.

Keywords: Institutions; Institutional Quality; Economic Development; Nigeria

JEL Code: B52, O10, O17. O55

1. INTRODUCTION

Institutions have become increasingly prominent in modern economies, and their importance has gained substantial momentum in the economic literature, particularly in explaining differences in economic performance and development outcomes across countries. Although institutions should not be regarded as synonymous with economic development, they constitute critical preconditions for sustainable growth because they establish the rules, norms, incentives, and governance structures that shape economic behaviour and the allocation of resources. Effective and qualitative institutions can enhance economic efficiency, promote equity, reduce uncertainty, strengthen incentives for productive investment, and facilitate the enforcement of contracts and property rights (Bakaret et al., 2015). In this regard, institutional quality influences the extent to which economic agents can participate confidently in productive activities and respond to market opportunities. Strong institutions therefore provide the rules and procedures necessary for coordinating economic activities and fostering sustained growth and development (Rothstein & Teorell, 2008). The significance of institutions to economic performance can be traced to the classical contributions of Adam Smith (1776), who emphasised the importance of justice, security, and effective government in creating an environment conducive to commerce and manufacturing.

From this perspective, economic activity cannot flourish where individuals and businesses lack confidence in the legal and governmental institutions responsible for protecting their rights and enforcing economic agreements. Differences in investment behaviour, productivity, and economic growth across countries can therefore be partly understood through variations in their institutional frameworks, particularly the extent to which property rights are protected, contracts are enforced, and the rule of law is maintained. Subsequent scholars further acknowledged the importance of institutional arrangements in shaping development outcomes (Lewis, 1955; Ayres, 1962), although systematic empirical investigation of the institutional determinants of economic performance emerged more prominently in the later development literature.

The growing empirical literature subsequently provided stronger evidence linking institutional quality to economic outcomes. Studies by Knack and Keefer (1995) and Mauro (1995), for instance, demonstrated the relevance of institutional quality, governance, and corruption to investment and economic performance. Similarly, Hall and Jones (1999) emphasised the importance of social infrastructure and institutions in explaining differences in productivity and output across countries, while Rodrik (1999) highlighted the role of institutional arrangements in determining the sustainability of economic growth. Acemoglu et al. (2002) further advanced the institutional perspective by demonstrating how differences in institutional structures can generate persistent differences in economic development. More recent evidence also reinforces the relevance of institutions to economic performance, particularly in developing economies where weaknesses in governance, regulatory quality, accountability, and enforcement mechanisms can constrain productive investment and undermine development outcomes (Lawal, 2021). Consequently, institutions should be understood not merely as administrative structures but as fundamental components of the economic environment that influence incentives, constrain opportunistic behaviour, facilitate investment, and shape the capacity of economies to achieve inclusive and sustainable development.

In this paper, we explore the concept of institutions from a non-explicable quantitative milieu following the introduction, the paper has the following structures, in section 2, and we survey what institutions are and what they are not. Institutional indicators are covered in section three. The institutional macroeconomic performance nexus is examined in section 4. The paper is concluded in section 5.

2. REVIEW OF LITERATURE AND CONCEPTUAL VIEWS

2.1. Institutions: What they are?

2.1.1 The Concept of Institutions

According to North (1990), institutions are the humanly devised constraints that structure political, economic and social interaction. Thus, institutions can be understood as the frameworks that establish and regulate the rules governing opportunities and incentives within an economic system. In the literature, the term institutions has been used to signify various characteristics of a country's socioeconomic and political setup.

From the foregoing, institutions are not only constraint that guide and structure interactions but also political and social relation which enhances Pareto-optimality positions for an economy. Acemoglu (2001) identified three important features arising from the definition as given by North (1990). First, institutions are humanly devised, in contrast with other potential fundamental causes such as

geographical factors which are basically outside human control. Second, they are the rules of the game which impose constraint on human behaviors. Third, the effects will be through various incentives in the economic system. In the light of this, the rules of the game are encapsulated in formal institutions (like laws and regulations) or informal settings (Tabellini, 2005).

The definition of institutions as rules, norms, and behavioural patterns, which are persistent and influence interactions, uncertainty and incentives for individual and collective actions, is broadly accepted. Lin and Nugent (1995) define institutions as rules and behavioural patterns that allow for stable expectations and Rodrik (2007) links good institutions with arrangements that foster economic growth, including regulatory institutions, property rights, macroeconomic stability, social insurance, and conflict management. Levchenko (2007) and Bretton (2004) highlight enforcement of contracts, protection of property rights and minimisation of the risk of expropriation as important aspects of institutional quality. Like Greif (2006), who sees institutions as systems of social factors, such as rules, beliefs, norms, and organisations which create behavioural regularities, or Glaeser et al. (2004), Leftwich (2006; 2007), and Hodgson (2006), who highlight their formal and informal, enduring attributes, and the way in which they structure social, economic, and political interactions. Ekpo (2013) also associates the level of institutional effectiveness with the ability of the State to maintain law and order, while Menard and Shirley (2005) emphasize the functions of institutions for providing certainty, transaction costs, and dealing with imperfect information and bounded rationality.

Institutions, from this point of view, are constraints and guidelines, formal and informal, emerging from political, economic and social interactions and aimed at improving the possibility of exchange, decreasing the costs of transactions and minimizing market failures. Institutions offer ways to coordinate behaviour and to minimize costs to social and economic exchange, as people and groups may have divergent interests. Institutions are also the results of historical and social developments and will, thus, change as the society changes. These can be written or unwritten in the form of laws, legislation, customs, traditions or socially accepted usage. In the traditional Nigerian communities there are some unwritten rules that have been in place for centuries which include marriage, worship, social relations and other parts of a traditional life. Institutions of all kinds are significant when they do promote behavior and produce positive social effects.

Also, the ability of institutions to correct market distortions and failures is a key criterion of institutional quality, not just a measure of how much they lower transaction costs. Property-right systems and other types of institutions should provide proper incentives and not over-concentrate economic opportunities and resources on specific groups. It should not be judged as good because it can increase economic growth; the impact on social and economic welfare and opportunity must also be taken into account (Acemoglu 2005). The efficiency of an institution is thus context-specific: what works for fostering development in one context may not function the same way in another socio-economic context. For example, unequal property rights could promote investment and growth, but also could raise inequality and consolidate economic and political power which can reduce the opportunities for broader engagement in the economy and politics. There is therefore a need to understand good institutions as context-specific arrangements that can facilitate inclusive economic opportunities, good governance and social welfare, but not as institutional templates to be exported from one society to another.

2.1.2 Types of Institutions

Institutions generally are divided into formal and informal institutions. According to the former, North (1990), formal institutions are written laws and regulations or contracts that are enforced via third parties, and informal institutions are socially shared behavioural norms and rules (Carey, 2000). Formal institutions offer institutional arrangements to govern the economic and social relationships, and to provide incentives for exchange (Rolland, 2003; Soysa & Jutting, 2007). Informal institutions, on the other hand, are unspoken rules, customs, conventions and codes of conduct that are part of a society's culture and social practices. These are frequently self-enforcing and hard to see and assess because they take place outside the official structures (Casson et al., 2010). Informal institutions existed before the formal institutions, but as the relationships in society and the economy started to grow more complex, credible commitments to the agreements and the prevention of market failures became a necessity, which led to the creation of formal institutions (Stiglitz, 2000). This distinction is thus relevant for empirical research since the formal institutions can be more easily observed than the informal institutions, which can have a major impact on individual and collective action, and because the formal institutions may be influenced by political considerations in which fairness matters as much as efficiency (Soltan, 1998).

Institutions can also be divided into economic institutions and political institutions, with the former having a greater influence on economic activities and the latter being more important in determining political power distribution and its utilization. Economics institutions affect investment, production, contract, property rights, markets exchange and competition. Formal economic institutions, for example, create and maintain property rights, ease the process of forming business organizations and organize transactions, and coordinate and compete in markets (Wiggins & Davis, 2006). Informal economic institutions are social norms, traditions and conventions that affect access to economic opportunity, cooperative efforts and the allocation of social and economic resources. They are linked closely to other social and political institutions and at times difficult to distinguish conceptually. Their economic importance is mainly due to the impact they have on incentives, on protection of property rights, and on market efficiency; secure property rights can induce investment and functioning markets can make it possible to allocate resources to productive use. Political institutions, in turn, will shape the acquisition, exercise, distribution, and control of political power. Formal political institutions include laws, constitutions, and rules of political authority and decision-making, as well as their operation and development, which are also shaped by informal political and social institutions.

2.1.3 Functionality on Institutions are Imperative to Good Definition

The performance of an institution – formal or informal – is best measured by its functional, efficient and ability to reach the goals it set for itself in a given social setting. Institutions vary in their ability to achieve the same results in different societies because of varying political, economic, cultural and historical contexts in different societies. Therefore, transplanting of western institutions without taking into account the local realities may not be appropriate. Consensus-oriented governance mechanisms, customary structures and culturally rooted leadership, as found in traditional governance systems in Nigeria such as Ife, Kano and Benin, show how consensus-based institutions can be legitimate and long-lasting. Likewise, formal financial institutions, predominantly interest- and collateral-based, may not be entirely suitable for the traditional values of need, reciprocity, cooperation and social responsibility practiced by some Nigerian communities. It highlights the need to construct institutions that are locally responsive, not only on the basis of an external institutional model. However, the question that faces us is not what form institutions take or whether they are Western or non-Western institutions, but whether

they are effective and considered legitimate and acceptable within the different contexts they operate in. Beyond institutional design, institutional effectiveness also relies on the level of trust, support and compliance of economic and social actors in the existing rules and practices. The more credible and transparent, reciprocal, and trustworthy institutions are, the more likely they are to enable cooperation and good implementation. Institutional quality thus has to be measured in terms of how well institutional arrangements – formal or informal – are able to deliver credible rules, mitigate uncertainty, facilitate cooperation and deliver socially desired outcomes in the particular socio-economic and historical setting in which they are embedded.

2.2 CLASSIFICATIONS OF INSTITUTIONS

There are three commonly known classification of institutions in the literature. These are classifications according to subject category, degree of formality and degree of embeddedness. Each of these classification on the average seeks, through in a different manner, to reflect institutional matrix (North, 1994) or the arena of actions (Ostroom, 2005). It need to be emphasize that irrespective of the classification type, the element of institutions usually intercept, both within and between the systems of classification. The implication of this is that, institution can be classifies in more than one way and this can be applicable even in a given type.

2.2.1 Subject Category

Under this classification, institutions may be legal, political, economic or social (Joskow, 2006). Legal institutions are the ubiquitous type of institution. This is because some form of law or legislature can be found in any kind of social interactions, no matter how primitive they maybe. Thus, a wide range of issues come under legal institutions, including property right, the origin and effect of legal structures, and enforcement of legislations. In terms of degree of formality classifications, legal institutions are a larger part of formal institutions.

Broadly speaking, political institutions involves the polity electoral regulation, voters, Political institutions include political parties as well as the rules that define and limit the powers of the state or government. Economic institutions, on the other hand, are those that promote and sustain an efficient and effective market system, such as the legal framework, property rights, their enforcement, and various forms of regulation. It is important to note that economic institutions are to a large extent shaped and influenced by political institutions. Social institutions encompasses concept including believes, norms and civil cooperation. They often coincides with informal institutions I n terms of degree of formality classification. Issues of social capital, their formations and role, and network also come within the purview of social institutions. Many social institutions are informal in nature and help shape private and communal behaviors, as well as interactions among individuals and groups. However, over time, formal institutions regulating social interactions and public behavior have also emerged and expanded.

Prominent in the literature is the inclination to regard and treat economy, social and political institutions as distinct, a tendency that has often led to the failure to recognize the often intertwine and overlap. Because of this, there is common failure by investigator in the institutional analysis to distinctly separate economic institutions from others, without due regards to the fact that economic institutions are inextricably political in their origin, impact and effect. Moreover, many investigators often fails to take into account that political institutions invariably affects the shape and functioning and economic institution.

2.2 Degree of Formality

This is the simplest classification of institutions and followed (Norths, 1990) definition. In the classification, there are only two distinct group's i.e. formal and informal institutions. Formal

institutions consist of laws (including statutory and common law or a combination of both), regulations, and other formally established rules to which individuals are explicitly required to adhere. In contrast, informal institutions comprise norms, conventions, codes of conduct, and trust-based practices that are not formally written down and therefore operate beneath the level of official documentation within society.

2.2.3 Degree of Embeddedness

This is Williamson's (1985) classification of institutions. Its characteristics features is that it describes the interlinking nature between formal and informal institutions using the concept of embeddedness. Under this, institutions are ordered in four levels, with varying degrees of embeddedness. Lower levels of institutions are considered to be more embedded so that their change is slower compared with higher levels of institutions. Level 1 is composed of vastly informal institutions such as traditions, norms, customs and religion. Level 2 institutions are less embedded, and are formal institutions or rules (e.g. the polity, property rights, judiciary and bureaucracy). Level 3 contains institutions of governance, in which the structures of governance are aligned with transactions and their associated costs. Level 4 institutions are mainly concerned with the rules governing the allocation of resources and employment. On the basis of the traditional or neoclassical principles of marginality which emphasize the maximization of objectives by economic agents, subject to certain constraint.

Due to the tendency for each higher level of classification system to evolve more slowly than the lower one, some frequencies of change have been proposed. For the first, the proposed frequency of change is from 100 to 1000 years. For the second, it is 10 to 100 years. For the third, it is 1 to 100 years. While for the fourth, changes can be on a continuous basis. Due to embeddedness, each immediate lower level constrains the immediate higher or less embedded level. While a feedback from higher to lower is possible, even though the constraining relationship is much stronger.

It is important to describe the relationship or interaction between formal and informal institutions. According to Helmke and Levitsky (2004), this affect outcomes (for instance macroeconomic performance) in four sterilized ways, i.e. complementary, accommodating, competing and substitution as shown in table 1

Table 1: Typology of Institutional Relationship Interaction

Outcomes	effective formal institutions	ineffective formal institutions
Convergent	Complementary	Substitutive
Divergent	Accommodating	Competing

Source: Helmke and Levitsky (2004, p. 728)

Formal and informal institutions are complementary when they converge and when formal institutions are effective. An example is when a country decides to establish better democratic rules and procedures. If there are already existing norms that act as some form of informal checks on abuse of political power, the content of the new laws may not matter very much. One scenario is that both laws might reinforce the check on power abuse or the formal laws. Another scenario is that there is likely to be an evolution of the formal law to become even a better check than what previously existed, as assort of benchmark is provided by the informal norm.

In the second typology, there may be accommodation of formal by informal institutions when the latter diverge and the former are effective, although it violates its sprit but not the latter. In the case, both

formal and informal institutions coexist and the outcomes of informal institutions are largely driven by informal institutions though such outcomes are not completely intended by formal regulations.

Third, when formal and informal institutions diverge and the former are ineffective, there may be competition between them. This is usually the case where a society has multiple source of justice and laws tend to compete among themselves, and in which formal laws are not well enforced. In many colonized states, there is the tendency for inherited laws to exist side by side with norms and tradition. Where there are infraction in some cases, the state may not feel the need to enforce formal laws and where willingness exists, the cost of enforcement may be too prohibitive. A good example is where formal laws protecting human rights may exist in the books, but in practice, customary laws act as a hindrance to their enforcement.

Last, where formal institutions are ineffective, informal institutions can take their place and substitute them. Thus, the informal institutions tend to be positioned to carry out the role of formal institutions which are largely ineffective. The esusu or informal contributory/ insurance schemes in Nigeria pass for this typology of interaction. Another example is the use of vigilante groups formed to prevent crimes in the absence of effective policy by official authorities. It is important to note that there is no question of competition, as these informal institutions do not pose serious threat to formal institutions, and in many cases are encouraged by the state.

2.3 INSTITUTIONS: WHAT THEY ARE NOT

It is important to distinguish between institutions and organizations, as the two concepts are often mistakenly used interchangeably, which can lead to confusion. In simple terms, institutions represent the “rules of the game,” while organizations are the “players” that operate within those rules. Failure to clearly differentiate between them has often prevented policymakers from fully appreciating the important role organizations play in shaping institutional arrangements. Organizations are crucial not only in maintaining institutions but also in modifying or even undermining them over time. Consequently, an inability to distinguish between institutions and organizations can limit policymakers’ capacity to design effective policies and frameworks that properly account for the interaction between the two.

Organizations refer to formally or informally coordinated groups through which individuals or collectives pursue shared goals and values. Like institutions, organizations can also be classified as formal or informal. In addition, their activities may operate within, across, or outside political, economic, and social institutional frameworks. In this context, formal organizations (as distinct from institutions) include entities such as companies, businesses, trade unions, political parties, and government ministries. Informal organizations, on the other hand, include groups such as criminal networks and secret societies, which typically have little or no public visibility and operate largely outside formal structures and codified rules.

3. METHODOLOGY

3.1 Institutional Indicators

Several variables are extant in the literature often used as an institutional indicators to measure the capacity of quality of institutions, with many of them related to governance, whether legal, political or economic. The most widely used indicators in the empirical literature are discussed.

3.2 Political Risk Index

The International Country Risk Guide (ICRG) index is a widely recognized publication produced by the Political Risk Services (PRS) Group. It incorporates a broad range of institutional indicators. One of its most prominent components is corruption, which has been extensively used in empirical research as a political economy factor influencing social pro-cyclicality. The overall ICRG index is constructed as the sum of 12 sub-indicators measuring different aspects of institutional quality. Different Scholars who have used these indicators includes Kutan and Zhou (1998) and Malik and Ahmed (1997). Crwoley and Loviscek (2002). Others include used individual components of the index, such as Rodrigues and Rodrick (1999), who used the “Bureaucratic Quality” measures, Saches and Warner (1995b), who employed the “Rule of Law” measures, and Acemoglu et.al (2001), who utilizes the “Risk of Exploration” measure.

3.3 World Governance Indicators (WGI)

This was propounded by Kaufaman, Zoido-Lobaton and Kray (1999), and often called the KKZ indicator, and Kaufmann, Kray and Mastruzzi (2003) with the first years of data being 1996-1997. The indicators are subsequently being updated yearly. They consist of composite indicators covering six broad dimensions of governance across more than 200 countries since 1996. These dimensions include: (1) government effectiveness, (2) regulatory quality, (3) rule of law, (4) voice and accountability, (5) political stability and absence of violence/terrorism, and (6) control of corruption. The six aggregate indicators are constructed from 31 underlying data sources that reflect the perceptions of a large number of survey respondents and expert assessments worldwide. The World Governance Indicators (WGI) serve as a benchmark that can motivate developing countries, such as Nigeria, to improve their governance performance. In particular, reducing corruption and improving living standards remain key priorities.

Conclusively, the lack of consensus among researchers on the most appropriate measures within the World Governance Indicators (WGI) framework makes drawing firm conclusions challenging. Government effectiveness, for example, captures the quality and availability of public services, the efficiency of the bureaucracy, the competence of civil servants, the degree of independence from political pressure, and the credibility and transparency of government policies and reform commitments. However, because the data are drawn from diverse sources, changes in the indicators may partly reflect revisions or corrections of previous estimates rather than real changes in governance. As a result, concerns have been raised about construct validity, meaning that the indicators may not fully measure what they are intended to capture. Consequently, some scholars argue that the WGI do not necessarily represent distinct concepts such as control of corruption, rule of law, government effectiveness, regulatory quality, political stability, and voice and accountability, but rather tend to reflect a single underlying broad governance dimension.

3.4 Economic Freedom of the World

The index of Economic Freedom introduced by Gwartney et al. (1996) serves as a general indicator of the quality of institutions in a country, including aspects of government size, sound money, international trade, legal structures and property rights, and regulation of credit, labour, and business. Empirical studies have associated economic freedom and institutional quality with macroeconomic results. Belke et al. (2005), in their study for selected countries in Sub Saharan Africa in the period 1989-2000, found that some measures

of economic freedom, especially the size of the government and the extent of market regulation, were determinants of exchange-rate outcomes. In a similar fashion, Qadir et al. (2012) found that business freedom was significantly affecting exchange rate stability in the case of Pakistan using OLS data from 2000 to 2010 and pointed out the relevance of institutional quality and investment in achieving economic stability. Aysun et al. (2013), who looked at 56 developed and developing countries, also concluded that financial and legal institutional conditions affected the effectiveness of monetary policy, with creditor recovery rates and legal origins being related to monetary-policy transmission. Despite this, the measurement of institutional quality is still subject of debate because notions of corruption, democracy, accountability, human rights, and other difficult-to-measure concepts cannot be captured in a consistent manner. While corruption is commonly linked to bad economic performance, especially in developing nations like Nigeria, it may also be a result of the interaction between formal institutions and informal norms, incentives, beliefs, political practices, and socioeconomic factors, and, thus, the solution to the problem is not a single institutional or public-sector reform.

3.5 Index of Civil Political Liberties

These two indices (index of civil and political liberties) published since 1973 by freedom house, measure that degree of civil and political liberties in a country. It is an attempt to look at activities “behind the scenes” as well as move away from objective measure of political institutions in order to examine the freedom of people in a country. An overall score of 17 is given to each index. The higher score reflected poorer liberties. Scully (1998). Levine and Renelt (1992), Sachs and Warner (1995a) and Isaham et.al. (1997) are some of the scholars who have used this measure of institutions.

3.6 Business Environment Risk Intelligence (BERI)

The Business Environment Risk Intelligence (BERI) index dates back to 1972. It comprises a risk index with ten components grouped into three main categories. The first category focuses on internal causes of political risk, including: (i) fragmentation of the political spectrum and the strength of competing factions, (ii) ethnic, linguistic, and religious divisions, (iii) restrictive measures used to maintain political power, (iv) societal attitudes such as xenophobia, nationalism, corruption, and nepotism, (v) social conditions such as population density and income distribution, and (vi) the organization and strength of groups advocating radical political change. The second category covers external causes of political risk, including (vii) dependence on or strategic importance to a major hostile power and (viii) negative influence from regional political forces. The third category captures symptoms of political risk, such as (ix) social unrest including demonstrations, strikes, and street violence, and (x) political instability manifested through non-constitutional changes of government, assassinations, and guerrilla warfare. With data on 53 countries, 26 of which are OECD countries investigators have tended to use other governance measures as the primary sources, while checking for robustness using the BERI index (Knack and Keefer, 1985; Svensson, 1998).

3.7 Second Generation Indicators

The second generation indicators were propounded by the World Bank, with collaboration with the committee on development assistant of the OECD, and the department of international development of

the government of United Kingdom. Some of the performance indicators have been identified reflecting, theses “Second generation indicators” and they include the following:

- (a). Enforcement of property rights (b). Policy unpredictability (c). Predictable judiciary
- (d). Budgetary volatility (e). Frequency of power outages (f). Contract intensive money
- (g). Number of independence business start-up procedure (h). Percent of the population expressing confidence in the state’s ability to protect them from crime (i). Number of independent legal actions to eject tenants (j). Revenue source volatility (k). Public perception of corruption in the public service (L). Quality of service delivery (m) contract enforcement (n) Regulation of entry (O) international trade tax revenue (p) waiting time for telephone line (q) percent of population fearful of crime.

3.8 Business International (BI)

The Business International (BI) index originally contained data from the period of 1971-1979 on 57 countries. Rising to data on 68 countries for 1980 to 1983. Since 1984, there has been wider coverage to include some 100 countries. The issues covered by the original BI index include the corruption index, bureaucratic efficiency (including the efficiency of the judicial system, as well as the absence of red tape and corruption), and political stability (reflecting institutional and social continuity, labour stability, relations with neighboring countries, and the presence of terrorism).The expanded index includes broader dimensions such as political stability, which covers war, social unrest, orderly transitions of government, politically motivated violence, and international disputes. It also includes political effectiveness, which captures pro-business orientation, institutional effectiveness, bureaucratic quality, transparency of the legal system, as well as levels of corruption and crime. Hines (1995), Tanzi and Devoodi (1997) and Wei (1997, 2000) have used this measures as primary indicator, while Gupta et.al, (1998) used it for robustness check result from the ICRG index.

3.9 Corruption Perception Index

The Corruption Perceptions Index (CPI), produced by Transparency International, has provided broad country coverage since 1995. It is constructed using data from multiple sources, including the Global Competitiveness Report, the World Competitiveness Yearbook, Information International (a survey of business people across 31 Middle Eastern economies), and the World Business Environment Survey. Additional sources include the Economist Intelligence Unit, Freedom House (particularly for transition economies), World Markets Research Centre risk ratings (covering issues such as red tape and corruption across 186 countries), and Columbia University’s State Capacity Survey, which compiles assessments from 224 U.S.-based country experts across 95 economies. Other contributing sources include the Political and Economic Risk Consultancy (PERC), PricewaterhouseCoopers’ Opacity Index (covering corruption perceptions in 34 countries), Gallup International surveys of senior business executives in 21 emerging economies, and the Business Environment and Enterprise Performance Survey (BEEPS), which collects corruption-related responses from approximately 6,500 individuals across 25 transition economies. Ng and Yeats (1991), Wei (2000) and Terrez (2002), are some of the scholars who have used this measures in their investigations.

Table 1; Proxies for Institutions

Panel 1: Economic Institutions

Measure	Proxy	Sources
Financial Freedom	Index of Economic Freedom	The Heritage Foundation
Business freedom	Index of Economic Freedom	WSI The Heritage Foundation
Regulatory quality	Regulatory quality	WB WGI
Economic of environment	freedom of the press	Freedom house
Credit market regulators	EFW index regulation of credit, labour and business	Fraser institute
Regulations of credit, labour And business labour market Regulations.	EFW Index	Fraser institute
Regulations of credit, labour and Business, Business regulation	EFW INDEX	Fraser Institute
Foreign ownership investment Restrictions	EFW INDEX	Fraser Institute
Capital control	EFW index	Fraser institute

Panel 2; Political Institution

Political environment*	Freedom of the press	Freedom house
Political rights*	Freedom in the world	Freedom House
Checks and balances	Checks and balances	WB
Democratic accountability	Democratic Accountability	ICGR
Corruption	Corruption	ICGR
Bureaucratic Quality	Bureaucratic quality	ICGR
Internal conflict	Internal Conflict	ICGR
Military in politics	Military in Politics	ICGR
Control of corruption	control of corruption	WB, WGI
Control of corruption index	Corruption Perception Index	Transparency international
Political Terror Scale	Political Terror Scale	Political Terror Scale

Panel 3: Legal Institutions

Property rights	index of economic freedom	the heritage foundation, WSI
Legal environment *	freedom of the press	Freedom house
Civil liberties*	freedom in the world	Freedom house
Judicial independence	EFW Index	Fraser institute
Impartial courts	EFW Index	Fraser institute
Protection of property rights	EFW Index	Fraser institute
	Law and order	ICGR
	Religion in politics	ICGR

Note; * the scale is inverse; a lower number implies higher quality and vice versa.

Sources; political risk services (2013); transparenvy international (2013); freedom house (2012a 2012b); worldbank (2013).

The evaluation of institutional quality highlights the importance of separating objective facts from perceptions and, at the same time, acknowledges governance indicators due to the widespread use of these indicators for empirical institutional research. Defining and measuring good governance is more difficult, however, as concepts like democracy, human rights and accountability are sometimes used as proxies for governance quality without good conceptual clarity. Despite this, institutional quality is seen as pivotal to economic results, as good political and economic institutions help to reinforce property rights, economic freedom, policy effectiveness and overall development. The literature also points to problems with the first generation institutional indicators, such as their lack of specificity and issues of political acceptability, and encourages the adoption of second generation indicators that are transparent, replicable, broadly applicable across country contexts, especially developing countries, accurate and consistently measured, clearly defined, and sufficiently independent from external factors not related to the institutional characteristics they are meant to capture.

3.10 Determinants of Institutional Quality in Nigeria

The importance of institutions for economic performance goes back to Adam Smith who pointed out that the rule of law, confidence in the justice system, and protection of property rights are critical for economic development, investment, and commerce. Previous scholars noted the role of institutions in affecting economic performance, but a systematic empirical study of the contribution of institutions to economic performance gained momentum in the literature in the following years (Lewis, 1995; Ayres, 1962; Knack & Keefer, 1995; Mauro, 1995; Hall & Jones, 1999; Rodrik, 1999; Acemoglu et al., 2002; Doucouliagos & Ulubasogly, 2006; Knowles & Weatherston, 2007; Fao, 2008; Abdel-Latif & Schmitz, 2009; Benishay & Betancourt, 2010; Cammack & Keilsall, 2010). The neoclassical growth model is useful for understanding the economic growth of capital, labour, savings, investment and technological progress, but it has a number of simplifying assumptions including free movement of goods and factors, perfect information and clearly established property rights that restrict its usefulness for explaining the institutional underpinnings of economic coordination and development. As a result, institutions are becoming more and more recognised as a means to solve the problem of imperfect information, transaction costs, coordination problems and uncertainty that affects economic behaviour.

The institutional perspective also indicates that the institutional environment is a set of formal and informal interlinked arrangements that can either facilitate or impede economic performance. There are various ways in which institutions function: as “rules of the game”, as a form of governance, and as a form of sustaining cooperation among economic actors. The rules-of-the-game view, as developed by North (1990, 1994), focuses on predictable behaviour, the enforcement of contracts, and sanctions, that can lead to more contracting and lower transaction costs (Wallis & North 1986). The governance-structure approach, based on Coase (1973) and Williamson (1975, 1985), centers on the governance structure, cooperation, hierarchy and how principal-agent problems are solved, whereas Axelrod (1984) highlights the importance of institutions facilitating cooperation, information sharing and sanctions

among self-interested agents. These views highlight how institutions can affect the performance of the economy in the long run through three mechanisms: decreasing transaction costs, improving contractual relations, and enhancing property rights, and providing incentives for productive economic activities.

Institutions gained greater salience as the failings of traditional economics models became more apparent, especially with respect to the experience of transition economies. Coase (1992) maintains that the institutional conditions of efficient markets, such as effective public policies, regulatory institutions, provision of public goods, social insurance, and conflict resolution, must be in place. The institutional view is therefore expanded beyond traditional economic factors, to include property-rights institutions, regulatory institutions, macroeconomic-stabilisation institutions and conflict-resolution institutions. Property-rights institutions impact on investment, saving, contracting, and economic incentives; regulatory institutions impact market failures, rent-seeking behaviour, anti-competitive behaviour and corruption; macroeconomic institutions impact on economic instability and policy-induced uncertainty and conflict-resolution institutions impact on inclusion, coordination, security and social stability (North, 1990; Rodrik, 2000). The quality of institutions can thus have impacts on economic performance in terms of incentives, uncertainty, resource allocation, investment choices and economic agents' capacity to undertake mutually beneficial transactions.

Overall, the literature suggests that institutional quality is an important determinant of economic development and macroeconomic performance. Effective institutions alleviate resource misallocation, enhance trust and social interaction, increase accountability, and foster conducive investment, innovation, and productive economic activity (Easterly & Levine, 2003; Kaufmann et al., 2004; Huther & Shah, 2005; Scully, 1992). There are also differences in the quality of institutions between countries, which have been linked to variations in economic development or international trade, including via contract enforcement and institutional quality of trading partners (Rodrik et al., 2004; Ranjan & Lee, 2003; Anderson & Marcoullier, 2002). In addition to the economic dimension, institutional quality has been correlated with health (Coleman, 1988; Helliwell, 2003; Knack, 2002; Coffe & Geys, 2005), education (Zak & Knack, 2001), financial accountability (Zak & Knack, 2001), public-service delivery (Grootaert, 2001), democratic practices (Tabellini, 2005), and higher economic wellbeing (Knowles & Weatherston, 2007), as well as with household income. Hence, institutions are essential elements of the development process, as they affect the ability of economic agents to coordinate with each other, establish trust, enforce rights, and carry out productive activities in an economy.

4. Institutions and Macroeconomic Performance

Institutions matter in understanding economic performance because of the idea of Adam Smith that the importance of confidence in the rule of law, the protection of property rights, and the confidence in the justice system for commerce, investment and economic development. Later, the institutional–growth connection began to be subjected to systematic empirical scrutiny, revealing that institutional quality can have an impact on investment, productivity, and long-run economic growth (Lewis, 1995; Ayres, 1962; Knack & Keefer, 1995; Mauro, 1995; Hall & Jones, 1999; Rodrik, 1999; Acemoglu et al., 2002; Doucouliagos & Ulubasogly, 2006; Knowles & Weatherston, 2007; Fao, 2008; Abdel-Latif & Schmitz, 2009; Benishay & Betancourt, 2010; Cammack & Keilsall, 2010). While the neoclassical growth model offers a useful starting point for analysing capital accumulation, labour, saving and technological progress, it makes a number of simplifying assumptions, such as frictionless exchange, perfect information and well-defined property rights, that constrain the scope of the model's application to understanding institutional and social conditions for economic coordination. Institutions are therefore

more relevant in the presence of imperfect information, transaction costs and lack of well-defined property rights among economic agents.

The institutional view focusses on the role of institutions as a network of formal and informal arrangements which can either enhance or hinder economic performance. There are three dominant ways of understanding this relationship: institutions as the “rules of the game”, governance arrangements, and the mechanisms for maintaining cooperative behaviour. From the first point of view, institutions can contribute to the predictability of transactions, to the reinforcement of contract enforcement and to the reduction of transaction costs, which can lead to more exchanges and investments (North, 1990, 1994; Wallis & North, 1986). The governance-structure perspective is related to the idea of ownership structure, cooperation, hierarchy and the solution of principal-agent problems (Coase, 1973; Williamson, 1975, 1985), while the cooperative-behaviour aspect is linked to the role of institutions in facilitating information exchange, trust, sanctions and cooperation between selfinterested economic agents (Axelrod, 1984). Coase (1992) also supports the view that markets need the right institutional context, in the form of suitable public policy, regulation, social insurance, mechanisms of conflict resolution and provision of social goods. These views show that, institutions affect economic performance by lowering uncertainty, transaction costs, enforcing property rights, promoting cooperation and offering incentives to the productive behavior.

Property-rights, regulatory, macroeconomic-stabilisation and conflict-resolution institutions are other ways of understanding institutional quality. Property-rights institutions affect investment and contracting by providing asset protection and reducing uncertainty, and regulatory institutions affect market failures, rent-seeking, corruption, and anti-competitive behaviour. Macroeconomic-stabilisation institutions help to mitigate economic volatility and uncertainty, while conflict-resolution institutions foster social inclusion, security, coordination, and peaceful resolution of political, social, and economic conflicts. Together, these institutional features help to manage resources efficiently, trust in each other's society, accountability, and sustainable economic performance (North, 1990; Rodrik, 2000). In general, empirical literature links better institutional development to better development and macroeconomic results, but the concept of good institutions is not always the same across various settings (Easterly & Levine, 2003; Kaufmann et al., 2004; Huther & Shah, 2005). Other dimensions of institutional quality are related to trade, public-service delivery, financial accountability, social cohesion, and economic wellbeing (Ranjan & Lee, 2003; Anderson & Marcouiller, 2002; Knack, 2002; Coffe & Geys, 2005; Zak & Knack, 2001; Grootaert, 2001; Tabellini, 2005; Knowles & Weatherston, 2007).

5. Conclusion

The objective of this paper is to explicate the concept of institutions from a non-quantitative perspective. Importantly, the various definitional orientations were examined and the conventional institutional indicators were discussed. The empirical investigations of the role of institutions on macroeconomic performance were emphasized. A common thread in the paper is that whenever definition or indicator employed. Institutions are fundamental to growth and development. However, it was argued that what is critical is the fundamentality of institutions and not whether they were developed in one place and transmitted to another. Thus, developing countries can and should have institutions that work for them, as long as they are legitimate, supported by all can be effectively implemented.

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