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Economic Governance Index

Measuring Economic Governance at District Level- The Concept Note

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"Good governance is perhaps the single most important factor in eradicating poverty and promoting development".

– Mr. Kofi Annan, Former General Secretary, UNO

Governance, as defined by the World Bank, is the manner in which power is exercised in the management of country's social and economic resources for development. It is a process which includes setting policies, programs and their implementation, enforcement and evaluation. It covers all the formal and non-formal actors involved in decision and policy making as well as the actions of implementation of these policies and decisions[1]. We define Economic Governance, as the nature and practice of economic management and ability to provide social, physical and institutional infrastructure and enabling environment for overall growth and development of households, industries and other stakeholders. Economic Governance is about how a government exercises its power in the management of social and economic resources for the region's development.

1. Importance of Economic Governance

The World Bank, in its research, has demonstrated the key link that exists between strong growth, good economic policy and high capacity states[2]. Strong economic governance is accepted as a key factor in building domestic and international confidence in an economy[3]. This confidence leads to more investment, generating more jobs. Good economic governance has the potential to reduce external risks and costs for businesses and households, leading to improved business climate and living standards. Better economic governance implies a conducive policy framework, better reach of infrastructure and other public goods and services, and an enabling law and order atmosphere with proper grievance addressing system.

[1]UNESCAP , "What is Good Governance?",
http://www.unescap.org/pdd/prs/ProjectActivities/Ongoing/gg/governance.asp.
[2] World Bank – World Development Report 1997.
[3] AusAID. "Economic Governance and the Asian Crisis" Quality Assurance Series.

2. Measuring Economic Governance

World Bank's Worldwide Governance Indicators (WGI) launched in 1996, addressed the issue of measuring the governance across the countries and provided reliable and comparable data on different aspect of Governance. It provided the methodology and insight which formed bases for many similar Indicators/Indices benchmarking and ranking economies and business climates. This World Bank initiative proved that different aspects of governance can be reliably measured.

There have been considerable efforts across countries to estimate the status of economic governance at different regions. The World Bank's "Doing Business" study, which is essentially a cross country comparative database on business climate existing in different countries, is a major effort. Recently, many countries have undertaken initiatives to establish governance/economic indicators for regions within the country to assess respective specific economic circumstances and use these findings / ranking for designing more effective policy and implementation plans.

2.1. Economic Governance Index: Measuring Enabling Environment

The Economic Governance Index (EGI) is essentially a measure of enabling environment provided by the local bodies for private enterprise and households. It is a comparative measure of the government influenced conditions under which the private enterprise and civil bodies (which affect business environment) operate. EGI is based on both objective data and users/stakeholders' experience survey data on socio-economic factors affecting a region.

EGI enables comparison of the socio-economic environment across regions, highlighting their strengths and weaknesses and provides a road map to policy makers and administrators as well as other stakeholders. EGI helps in creating a proactive and competitive process aimed at improving the local business and social environment as it provides data and benchmarks to enhance transparency and accountability.

EGI adopts an index-based approach for measuring socio-economic environment, as this approach

- provides indicators which can measure and benchmark different aspects of governance and help in monitoring progress
- highlights constraints to economic growth

3. International experience in building Economic Governance Index

Several Asian developing countries have incorporated Economic Governance Index or its variants in their governance policy to improve local economic governance, business environment and provide framework for local administrators. Vietnam's Provincial Competitiveness Index (PCI) launched in 2005, focusing economic governance and private sector development, is considered very effective by international NGOs and business communities as it provides guidelines and helps in prioritizing interventions and many donor projects consider PCI as central to their efforts.

The success of Vietnam Competitiveness Index has resulted in several other developing countries adopting similar indices to meet their demand for effective diagnostic and guiding tool for local economic governance. Cambodia's Provincial Business Environment Scorecard (launched in 2006), Philippines' Good Governance Index and Indonesia's One Stop Shop Performance Index are some major initiatives aimed at measuring different aspects of economic governance and business climate. India, too, came up with similar studies and indices at national level addressing different aspects of Indian social and business environment.

4. Need for district level economic governance in India

The existing national indices or studies done at higher levels fail to highlight variations, strengths and weaknesses within the state or at lower level. Any state's overall performance on

Potential Users of Economic Governance Index

- Government
    - Policy Planning
    - Benchmarking
    - Prioritization of Interventions
- Investors and Business Houses
    - For making investment decisions
- Donor Agencies and Development Organization
    - Project Planning
    - Policy Advocacy
    - Benchmarking
- Academicians and Researchers

these indices or studies might not reflect the better performing districts or units within a state. Moreover, state is too large a unit and so state averages are too crude indicators and do not show variance. Some districts in low ranked state can be better governed than some districts in high ranked state. Sub-state approach seems to be focused on clusters, and cluster studies have its limitations as they are more focused on individual sub-sectors or industry not reflecting the overall potential.

The Economic Governance Index highlights and captures sub-regional disparities and provides a framework for sub-regional planning and prioritization of interventions. Being based on users/stakeholders experience survey data as well as on objective data, it presents a holistic scenario to stakeholders (namely, Government. organizations, investors, civil society organizatons etc.) and helps them in informed decision making.

Even among fast growing states, there is a need to identify alternate districts that could accommodate businesses and reduce the pressures on the main district of the state (usually the capital city). EGI helps identify such districts for the business community, and give a picture on what needs to be done to promote districts that lag behind.

Benchmarking is one of the crucial factors in governance planning and EGI can act as benchmarking tool providing information on different factors/indicators of economic governance. EGI helps in sub-national policy making and benchmarking best practices.

4.1. Economic Governance Index: Ingredients

The proposed District Economic Governance Index (EGI) is an effort to quantify the local business environment and factors contributing/affecting investment, growth and business environment at district level and providing benchmarks and standards to policy makers, administrators, investors and other stakeholders. The EGI effort proposed by the Centre for Development Finance, IFMR, is different from other governance indexing approaches followed elsewhere, in the sense that the user/stakeholder survey would cover the household sector too, so that the reach of public goods is effectively reflected in the survey.

The EGI will consist of the following sub-indices.

Physical Infrastructure: Good infrastructure facilitates access to factor and product markets, thereby raising productivity and profitability. Accordingly, both domestic and foreign businesses are attracted to areas with adequate roads, ports, telecommunications facilities, and power and water supply, as shown by earlier research[4]. Quality infrastructure services significantly affect a firm's profitability via reduction in production costs and ability to reach wider markets. Infrastructure is also an outcome measure of governance and reflects effectiveness of policies and implementation.

Social infrastructure: Social infrastructure is about providing basic support, particularly healthcare facilities and schools for children. This is indispensable for creating a quality manpower base in a region.

Business Establishment Cost: Business Establishment Cost is measure of time taken by firms to register, acquire land, obtain all necessary licenses and complete procedures to start business and perceived degree of difficulty to obtain licenses and permits.

Governance and Regulatory Environment: Governance and Regulatory environment is one of the major factors influencing investment decisions and investment climate. Good governance institutions are viewed as reducing uncertainty, as well as the cost of doing business. Good regulator environment is also important to reduce compliance costs. A conducive regulatory environment implies that local governments have a positive attitude towards businesses.

Law and Order: Strong and effective law and order guarantee the security of foreign and domestic investments. They also create many positive externalities for productivity and growth. Availability of legal institutions to settle disputes is an important business consideration.

Cost of Doing Business: Local taxes, informal charges and other location differences in running business affect investment and related decision in major way.

Environmental sustainability: Un-regulated growth of industry can lead to degradation of the local environment and this poses serious risks – short-term and long-term – for the local populace. It is important to measure the environmental sustainability of the region to make a meaningful analysis and to ensure that the governance programmes are sustainable over the long run and are least risky to the population. Parameters such as forest-cover, water-table, waste disposal and sanitation form important part of this sub-index.

4 Herrin, Alejandro N., and Ernesto M. Pernia. 1987. Factors Influencing the Choice of Location: Local and Foreign Firms in the Philippines. *Regional Studies* 21(6): 531-541.

The following table provides tentative list of indicators used to develop the above sub-indices. It may be adjusted based on data availability.

Table 1: Tentative List of Sub-indices and Indicators

	Sub-Indices	**Indicators**
1	Physical Infrastructure	• Roads • Electricity • Water • Telephony • Railway network • Banking network
2	Social infrastructure	• Schools /Colleges • Teachers • Hospitals • Medical professionals
3	Business Establishment and Regulatory Compliance Cost	• Time taken to register a new business • Number of Licenses and Permits required to start operation • Time taken to acquire land • Stamp duty for registration of land, building • Access to Finance • Productivity Loss due to regulatory processes/inspections
4	Law and Order	• Legal Institutions enforcing law/contracts • Conflict Resolution Efficiency • Cases Pending in Court • Police personnel Availability • Crime statistics, nature of crime
5	Governance	• Administrative Quality • Transparency • Public Accountability • Efficiency of local government in delivering services • The experience of business community about the local government and its attitude towards business

6.	Cost of Doing Business	• Taxes • Informal Charges
7	Environmental sustainability	• Forest cover • Ground-Water tables • Waste disposal

5. Methodology

The methodology for constructing the District Economic Governance Index involves three steps.[5]

Step 1: Data Collection -The first step in data collection would be explore the existing secondary data available (data collected by existing government bodies, publications etc.) and assess the gap between data available and that required for constructing sub-indices. Most important here is data generated out of the users/stakeholder survey.

Step 2: Processing collected data to construct sub-indices -The collected data would be processed using statistical tools. Indicators for each sub-index would be standardized and aggregated to create sub-indices.

The aggregation methodology will draw on literature developed for a larger set of indices that are increasingly being used to identify priority areas for public and private investment as well as assess growth, development, and other aspects of government performance.

Step 3: Constructing the Final EGI-Since all the sub-indices do not contribute equally to competitiveness, growth and development, multivariate regression analysis would be used to decide the weights of these sub-indices. The final EGI would be on a 100 point scale to measure the governance of individual districts

[5] This methodology is being fine tuned and a pilot study is going on for preparing the final list of indicators and deciding weight of each sub-indices.