Does Good Governance Matter? Kazakhstan's Economic Growth and Worldwide Governance Indicators

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Abstract

Good governance is generally believed to improve country's economic performance. This paper studies the relationship between the World Bank's Worldwide Governance Indicators (Voice and Accountability, Political Stability and Absence of Violence, Government Effectiveness, Regulatory Quality, Rule of Law, Control of Corruption) and economic growth in terms of GDP per capita in Kazakhstan. The findings of the research indicate that there is a significant positive relationship between good governance and economic performance of Kazakhstan. Specifically, results show that the Control of Corruption has the strongest impact on GDP per capita.

Keywords: Good Governance; Worldwide Governance Indicators; Corruption; Economic Growth

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INTRODUCTION

Economic growth is one of the most important instruments in improving the quality of life of people, especially in developing countries. Growth often indicates improvements in creating opportunities for entrepreneurship which drives prosperity of a nation. Inclusive and sustained economic growth creates more jobs for society, increases income levels, leads to improvements in health and education and reduces the level of poverty. As Dani Rodrik (2007) claims, "historically nothing has worked better than economic growth in enabling societies to improve the life chances of their members, including those at the very bottom". There is no magic formula that countries can use to ensure sustainable economic growth and become more developed countries. At the same time, scholars, international donor organizations, policymakers and civic societies in general tend to agree that the quality of governance matters a great deal for economic development and hence the economic growth of a country (Lahouij, 2016). A "good" governance creates many dividends for societies - higher literacy rate, industrialization, income, longer life expectancy, lower infant mortality and others (Pelizzo & Stapenhurst, 2013).

There are many definitions of governance. One of the most popular ones was proposed by Kaufman et al (1999), who defined the term as "the traditions and institutions by which authority in a country is exercised". According to the authors, governance includes such aspects as the process by which governments, are selected, monitored and replaced, their capacity to formulate and implement effective policies, and the recognition and acceptance of the institutions that shape social and economic interactions by the citizens and the state. An earlier definition developed by the World Bank (1992) is that "governance is the manner in which power is exercised in the management of a country's economic and social resources for development". Francis Fukuyama (2013) defines governance as "government's ability to make and enforce rules, and to deliver services, regardless of whether that government is democratic or not". Moreover, he discusses two separate dimensions that can measure the quality of governance – (1) capacity, that "consists of both resources and the degree of professionalization of bureaucratic staff", and (2) autonomy, "the manner in which the political principal issues mandates to the bureaucrats who act as its agent".

As many definitions of governance there exists, naturally, there are also many notions what constitutes a "good governance" and how it can be measured. For instance, according the UNDP (1997):

"Good governance is, among other things, participatory, transparent and accountable. It is also effective, equitable, and it promotes the rule of law. Good governance ensures that political, social, and economic priorities are based on broad consensus in society and that the voices of the poorest and the most vulnerable are heard in decision-making over the allocation of development resources".

The Worldwide Governance Indicators (WGI) developed by Kaufman et al (1999) are probably the most widely used indicators to measure and compare the quality of governance. The WGI report for over 200 countries and territories since the period of 1996 on six broad dimensions of governance, voice and accountability, political stability and absence of violence, government effectiveness, regulatory quality, rule of law, and control of corruption.

Kazakhstan is one of the most oil-rich countries in the Central Asia. Since gaining independence in 1991, Kazakhstan's economy has grown by nearly 7 times, and real per capita income has increased by 3.6 times (The World Bank Data, 2019). The long-term goal of Kazakh-

stan, set by the first President, Nursultan Nazarbayev, in the Strategy "Kazakhstan-2050" is to enter the top-30 most developed countries of the world. In 2015, Nazarbayev outlined 100 concrete steps to achieve this goal, which focused on the realization of 5 institutional reforms, three of which are directly concerned with improving the quality of governance: the development of professional civil service, ensuring the rule of law and establishing an accountable state. These documents seem indicate that the political authority in Kazakhstan recognizes the role of good governance in the development goals of the country, especially after the oil price shocks in 2014.

The aim of this paper is to explore the relationship between the World Bank's good governance indicators and Kazakhstan's economic growth in terms of GDP per capita. In doing so, this paper is divided into the following sections: first, the WGI indicators are briefly explained and a brief overview on Kazakhstan's performance on the WGI is given. Next, existing literature on the relationship between good governance indicators and development indicators is discussed. Then the methodology of this research paper is described. This is followed by the results and discussions section. Finally, some concluding remarks and recommendations are drawn.

The Worldwide Governance Indicators and Kazakhstan's Performance

In 1999, World Bank's economists Kaufman, Kraay and Zoido-Lobaton published an influential paper that found empirical evidence on a significant causal relationship from better governance to better development outcomes based on cross-section data analysis of more that 300 indicators covering more than 150 countries. They developed six aggregate governance indicators using unobserved components methodology (Kaufman et al, 1999). According to the official website of

the World Bank (2019):

These aggregate indicators combine the views of a large number of enterprise, citizen and expert survey respondents in industrial and developing countries. They are based on over 30 individual data sources produced by a variety of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms.

Table 1 summarizes the dimensions, definitions and some of the main sources of each indicator based on Kaufman et al (2010).

In terms of Kazakhstan's performance in the WGI, Knox and Janenova (2018) characterize it as "a mixed bag". Figures 1-6 show how Kazakhstan's governance scores have been changing over the course of 20 years. It can be said that over the period of 1996 through 2017, Kazakhstan has significantly improved in government effectiveness which measures the quality of public services and capacity of the civil service. Some improvements are seen in regulatory quality and the rule of law. There is a little improvement in the control of corruption. Political stability has been the most volatile among the other, but in general has been stable for the last 4 years. Finally, the voice and accountability score is the only indicator that has become marginally worse over the whole period.

Literature Review

Good governance has lately been seen as one of the most significant factors for sustainable economic growth and development in academic literature. Alesina et al (1996) studied the relationship between political instability and growth of the GDP per capita for the data of 113 countries over the years of 1950-1982. They find that political instability negatively affects economic growth. Feng (1997) finds similar results for the data of 96 countries over 1960 through 1980. governance to per capita income. Moreo-

Table 1. WGI definitions and sources

Source: Kaufman et al, (2010)

Indicators	Definitions	Selected sources
The processes by which governments are selected, monitored, and replaced:		
Voice and Accountability	capturing perceptions of the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media	Freedom House, Global Competitiveness Report, Gallup, Economist Intelligence Unit, Global Integrity Index, Political Terror Scale
Political Stability and Absence of Violence	capturing perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including politically motivated violence and terrorism	Global Competitiveness Report, Economist Intelligence Unit, Political Terror Scale
The capacity of the government to effectively formulate and implement sound policies:		
Government Effectiveness	capturing perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies	Global Competitiveness Report, Gallup, Enterprise Surveys, ADB, Economist Intelligence Unit, Global Integrity Index
Regulatory Quality	capturing perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development	Global Competitiveness Report, Enterprise Surveys, EBRD, ADB, Economist Intelligence Unit
The respect of citizens and the stat for the institutions that govern economic and social interactions among them:		
Rule of Law	capturing perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence	Freedom House, Global Competitiveness Report, Gallup, Enterprise Surveys, Economist Intelligence Unit, Global Integrity Index
Control of Corruption	capturing perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests	Freedom House, Global Competitiveness Report, Gallup, Enterprise Surveys, Economist Intelligence Unit, Global Integrity Index

Hall and Jones (1998) found that a country's long-run productivity, capital accumulation, productivity per worker are most dependent on institutions and policies by the government. Since Kaumfan et al's publication in 1999 that showed positive correlation between good governance and development, many studies have followed, mostly with similar result.

Chong and Calderoan (2000) found significant causal relationship between institutional quality and economic growth. They went on to argue that improving insti-tutional quality which includes better property rights, reducing corruption and uncertainty takes long time to achieve economic development.

In 2002, Kaufman and Kraay once again studied the relationship between the WGI and per capita income, covering over 175 countries for the period of 2000 and 2001. They found that good governance is necessary for high income per capita. Following their methodology, Emara and Jhonsa (2014) found a positive, strong statistically significant causation from quality of

ver their results suggest a positive causation from per capita income to quality of governance for 22 Middle East & North Africa (MENA) countries.

Lahouij (2016) used panel data for 2002-2013 to investigate the impacts of governance and other economic growth determinants on economic growth of some selected oil-importing MENA countries and found that governance is strongly associated with the economic development.

Hyunh and Jacho-Chavez (2009) examined empirical relationship between governance and economic growth using nonparametric quantile methods and found that voice and accountability, political stability, and rule of law are significantly correlated with economic growth.

Asian Development Bank's Han et al (2014) studied whether countries with above-average governance grew faster than countries with below-average governance. The have found that government effectiveness, political stability, control of corruption and regulatory quality all have a more significant positive impact on country growth performance than voice and accountability and rule of law. Moreover, their findings suggest that in Asia, developing countries with above average government effectiveness, regulatory quality and corruption control grew faster than those with below average scores.

Campos and Nugent (2002), in turn, tested for a causal and negative long-run relation between political instability and economic growth but finds no evidence of such a relationship, based on data between 1960 and 1995, for 98 developing countries. However, Aisen and Veiga (2013) found quite the opposite, suggesting that higher degrees of political instability are associated with lower growth GDP per capita rate, by using the system-GMM estimator for linear dynamic panel data models on a sample covering up to 169 countries, and 5-year periods from 1960 to 2004.

Acemoglu et al (2005) developed empirical case that differences in economic institutions are the fundamental cause of differences in economic development. They conclude that economic institutions cause economic growth when political power is allocated to groups that enforce propriety rights, when they create effective constraints on power-holders, and when there are relatively few rents to be captured by power-holders.

Zubair and Khan (2014) explored relationship between WGI indicators and economic growth (GDP) using estimates related to Pakistan and found that political stability contributes the most towards economic growth of Pakistan.

Pelizzo and Stapenhurst (2013) suggest that corruption is not only associated with lower levels of socioeconomic development, but that there is a significant causal effect of corruption on a country's level of socioeconomic development.

Grindle (2004, 2007), on the other hand, argues that the notion of 'good governance' falls short of being a tool to explore what, specifically, needs to be done in a real world context and provides "little guidance about what's essential and what's not, what should come first and what should follow, what can be achieved in the short term and what can only be achieved over the longer term, what is feasible and what is not". Morita and Zaelke (2007) found that rule of law and good governance are important to achieve sustainable development; however, it is also important to ensure the implementation of laws and rules rather than just making the laws and regulations.

It can be concluded that, the majority academic literature on exploring the relationship between good governance and economic development tends to suggest that there is a significant positive relationship between those. While there is extensive amount of literature available for cross-country analysis and time-series analysis for some countries and groups of

countries such as OECD, MENA, Asia and others, there was not found any academic research on the relationship between good governance and economic growth for Kazakhstan. This paper aims to fill that gap.

RESEARCH METHODS

This research was based on quantitative approach to explore whether there is a significant relationship between WGI and economic growth rate of Kazakhstan, and if yes, how strong is the relationship. In order to do that, secondary time-series data was collected for WGI and GDP per capita of Kazakhstan. The timeline involves 19 years of available data: 1996, 1998, 2000, 2002-2017. Odd years till 2003 are omitted because until then WGI were collected only once in 2 years.
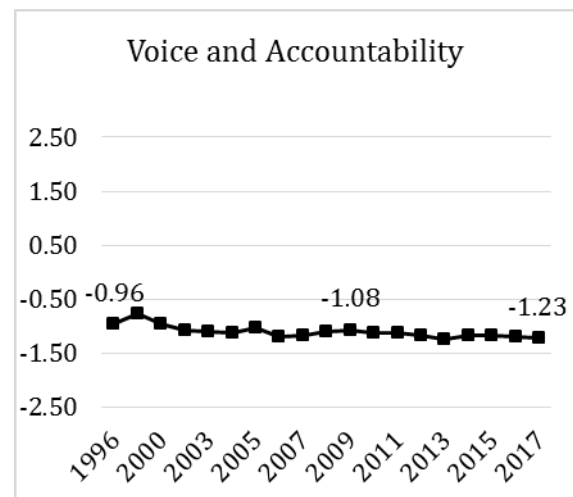
Independent Variables

Initially, all the six dimensions of

Figure 1. Political Stability and Absence of Violence scores for Kazakhstan
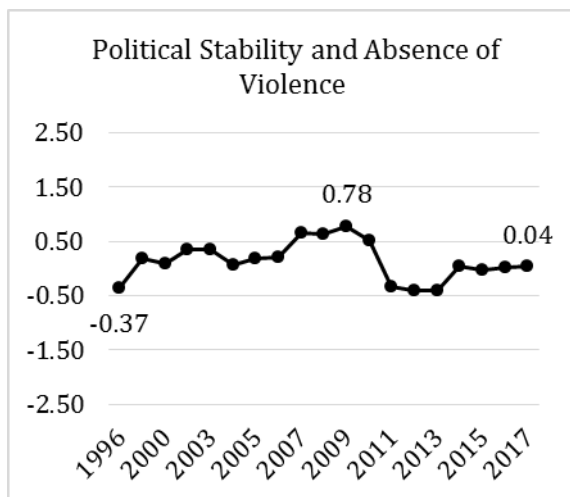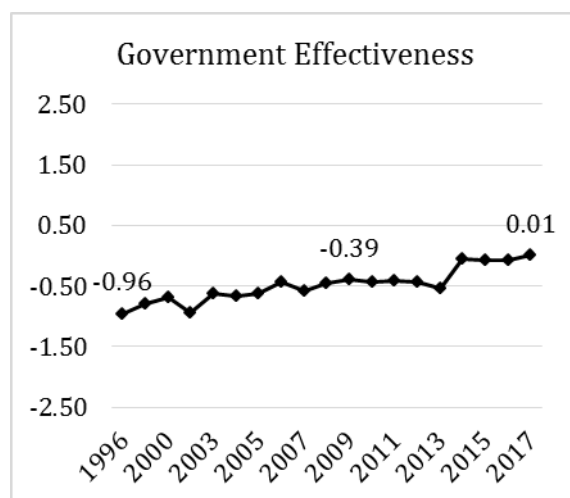

Source: World Bank (2017)

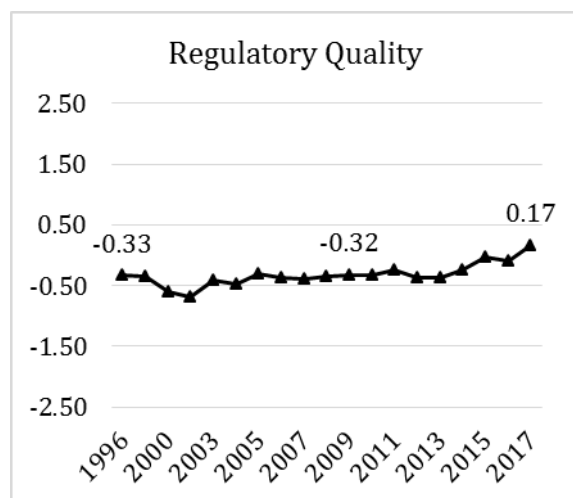Figure 2. Voice and Accountability Scores for Kazakhstan

Source: World Bank (2017)

Figure 3. Government Effectiveness scores for Kazakhstan

Source: World Bank (2017)

Figure 4. Regulatory Quality Scores for Kazakhstan

Source: World Bank (2017)

WGI were considered in this research. Taking into account the data normality and multicollinearity issues, that are tested in the Results and Analysis section, the following independent variables are selected, political stability and absence of violence (ps), regulatory quality (rq), and control of corruption (cc). The data for the WGI were collected from the World Bank database.

Dependent Variable

GDP per capita in current dollars (GDP per capitat) is selected as a dependent variable. It measures country's economic output accounting for population size. GDP per capita is considered to be one of the most important indicators that measures prosperity and standard of living in a country. The data for Kazakhstan's annual GDP per capita is gathered from the World Bank Database as well.

Taking into consideration that the annual WGI scores are constructed including the data collected in a year before, corresponding previous year's GDP per capita (GDP per capitat-1) is also tested as a dependent variable.

The models are as follows:

GDP per capitat = β_0 + β_1 PSt + εt,

GDP per capitat-1 = β_0 + β_1 PSt + εt;
GDP per capitat = β_0 + β_1 RQt + εt,
GDP per capitat-1 = β_0 + β_1 RQt + εt;
GDP per capitat = β_0 + β_1 CCt + εt,
GDP per capitat-1 = β_0 + β_1 CCt + εt;
GDP per capitat = β_0 + β_1 PSt + β_2 CCt + εt,
GDP per capitat-1 = β_0 + β_1 PSt + β_2 CCt + εt,

Where PS_t refers to the score of Political Stability and Absence of Violence for year t, RQ_t refers to the score of Regulatory Quality for year t, CC_t refers to the score of Control of Corruption for year t, β_0 denotes intercept parameter, β_1, β_2, β_3 denote regression parameters and ε_t denotes unobserved error term for year t.

Hypotheses

The following hypotheses are tested in this paper:

- H0 (a): There is no relation between Political Stability and Absence of Violence and GDP per capita.
- H1 (a): There is a positive relation between Political Stability and Absence of Violence and GDP Growth Rate.
- H0 (b): There is no relation between Regulatory Quality and GDP Growth Rate.

Figure 5. Rule of Law scores for Kazakhstan
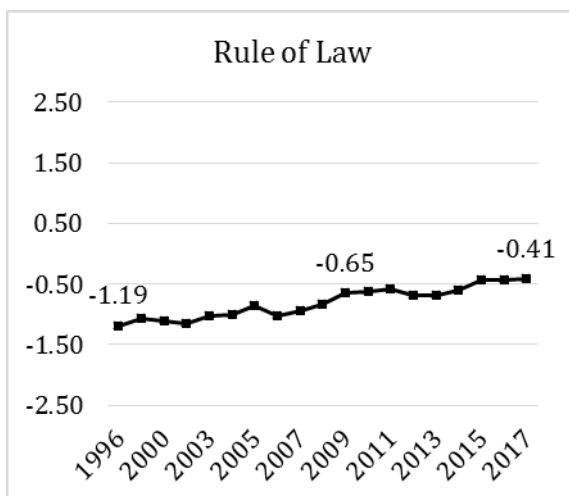
Source: World Bank (2017)

Figure 6. Control of Corruption for Kazakhstan
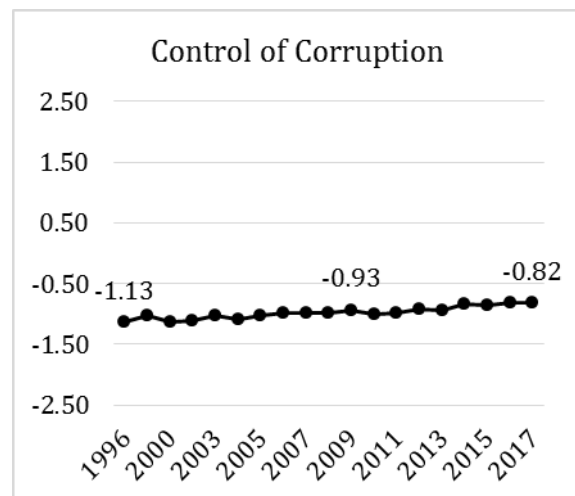
Source: World Bank (2017)

- H1 (b): There is a positive relation between Regulatory Quality and GDP Growth Rate.
- H0 (c): There is no relation between Control of Corruption and GDP Growth Rate.
- H1(c): There is a positive relation between Control of Corruption and GDP Growth Rate.
- H0 (d): Full Model is insignificant.
- H1 (d): Full Model is significant.

RESULTS AND DISCUSSION
Data and Summary Statistics

Table 2 displays the descriptive statistics for each variable. It shows that the average GDP per capita adjusted for the previous year (t-1) is slightly lower than the average of the corresponding GDP per capita (t). This is because Kazakhstan's GDP per capita was the lowest (1130 USD) in 1999. The highest GDP per capita (13890) was achieved in 2013. It can also

Table 2. Summary Statistics
Source: Processed by the Author (2020)

Variables	Observations	Mean	SD	Min	Max
GDP per capita (t)	19	6800.34	4305.02	1229.00	13890.63
GDP per capita (t-1)	19	6393.84	4445.44	1130.11	13890.63
Voice and Accountability	19	-1.105	0.114	-1.243	-0.764
Political Stability and Absence of Violence	19	0.135	0.358	-0.408	0.777
Government Effectiveness	19	-0.481	0.283	-0.958	0.006
Regulatory Quality	19	-0.321	0.189	-0.696	0.170
Rule of Law	19	-0.804	0.257	-1.187	-0.411
Control of Corruption	19	-0.978	0.099	-1.133	-0.817

Table 3. Normality Test (Skewness/Kurtosis)
Source: Processed by the Author (2020)

Variables	Pr (Skewness)	Pr (Kurtosis)	Joint (prob>Chi2)
GDP per capita (t)	0.849	0.040	0.111
GDP per capita (t-1)	0.591	0.032	0.086
Voice and Accountability	0.005	0.022	0.006
Political Stability and Absence of Violence	0.922	0.506	0.791
Government Effectiveness	0.635	0.722	0.836
Regulatory Quality	0.171	0.082	0.087
Rule of Law	0.866	0.027	0.087
Control of Corruption	0.763	0.422	0.675

be concluded that Kazakhstan, on average, is doing relatively better in terms Political Stability and Absence of Violence but worse in terms of Voice and Accountability. In terms of the Control of Corruption, the difference between the highest (2017) and the lowest score (1996) is 0.32 which is relatively small.

Before running correlation and regression tests in order to examine the relationship between the WGI and GDP per capita, the data is checked for normality and multicollinearity. Table 3 shows the normality test results.

It can be concluded that the data for all of the variables except for the Voice and Accountability are normally distribut-

ed since the P-values of the joint test are greater than the significance level (0.05). Based on that, the Voice and Accountability variable is dropped from the analysis.

Table 4 shows the Multicollinearity test results. It shows that Government Effectiveness, Rule of Law, Regulatory Quality and Control of Corruption are highly correlated between each other, thus all indicators but Political Stability and Control of Corruption could be omitted from the analysis. However, Regulatory Quality is decided to be included in the correlation test and simple regression analysis to examine which of the three variables is a stronger predictor. However, it is then omitted when the Full Model will be ana-

Table 4. Multicollinearity Test
Source: Processed by the Author (2020)

	Political Stability	Government Effectiveness	Regulatory Quality	Rule of Law	Control of Corruption
Political Stability	1.000				
Government Effectiveness	-0.054	1.000			
Regulatory Quality	-0.192	0.795	1.000		
Rule of Law	-0.151	0.902	0.789	1.000	
Control of Corruption	-0.096	0.926	0.793	0.890	1.000

Table 5. GDP per capita and WGI Correlations.
Source: Processed by the Author (2020)

(N=19)	GDP Per Capita		
	Spearman's Rho Correlation coefficient (t-1)	P-Value (t-1)	Result
Political Stability and Absence of Violence	-0.374 (-0.374)	0.115 (0.115)	Fail to reject H0 (a)
Regulatory Quality	0.497 (0.583)	0.031 (0.009)	Reject H0 (b)
Control of Corruption	0.805 (0.895)	0.000 (0.000)	Reject H0 (c)

lyzed.

Correlation Test

Spearman's Rho Correlation test is used in this paper in order to find the relationships between GDP per capita and the WGI and to examine their significance. This type of test is selected in an attempt to replicate Zubair and Khan's (2014) study on the relationship between GDP and the WGI in Pakistan. Table 5 shows the results of the correlation test. The values in brackets show the test results for the adjusted GDP per capita (t-1).

Correlation of the GDP per capita and Political Stability and Absence of Violence is insignificant at 5% significance level under both scenarios; hence, $H_0(a)$ cannot be rejected. The correlation coefficient for Regulatory Quality is also insignificant under unadjusted GDP per capita (t); however, with the adjusted GDP per capita (t-1) it is calculated to be 0.583 which is significant at 5% significance level. Based on that, $H_0(b)$ is rejected, meaning that there is a positive relationship between the Regulatory Quality and the adjusted GDP per capita. Finally, the results suggest that there is a strong positive and significant relationship between

Table 6. Linear Regression Analysis Output
Source: Processed by the Author (2020)

	Political Stability and Absence of Violence (t-1)	**Regulatory Quality (t-1)**	**Control of Corruption (t-1)**
P-Value	0.214 (0.231)	0.032 (0.015)	0.000 (0.000)
R^2	0.089 (0.083)	0.242 (0.299)	0.565 (0.716)
adj. R^2	0.036 (0.029)	0.197 (0.258)	0.539 (0.699)
Cons. (β_0)	7286.7 (6878.9)	10392.6 (10518.9)	38504.3 (43255.4)
Coeff. (β_1)	-3593.8 (-3584.9)	11179.6 (12837.9)	32431.4 (37707.3)

Table 7. Full Model Results
Source: Processed by the Author (2020)

(N=19)	**Coefficient (t-1)**	**P-Value (t-1)**	**R^2 (t-1)**	**adj. R^2 (t-1)**
Political Stability and Absence of Violence (β_1)	-2749.3 (-2597.2)	0.161 (0.109)		
Control of Corruption (β_2)	31481.1 (36810.6)	0.000 (0.000)		
Cons. (β_0)	37947.4 (42730.3)	-		
Full Model	-	0.0005 (0.0000)	0.616 (0.759)	0.568 (0.729)

Control of Corruption and GDP per capita of Kazakhstan, both adjusted and unadjusted. Thus, $H_0(c)$ is rejected.

Linear Regression Analysis

It would be interesting to test the relationship between the variables in order to examine how strong are the predictors under different scenarios. Table 6 shows the results of the regression analysis conducted separately with each independent variable.

The regression analysis produces fairly similar results as the correlation test. Political Stability and Absence of Violence is insignificant for GDP per capita in Kazakhstan under both scenarios since the p-values are exceeding the significance level (0.05).

Regulatory Quality, however, is significant at 5% significance level under both GDPs per capita, although the adjusted one provides stronger result. The coefficient β_1 for Regulatory Quality implies that, for instance, with 0.1 point improvement in the score the GDP per capita for the same year that the indicator is based on (the year of data collection) is expected to increase by 1284 USD, while for the next year (the year when the score is published) it is expected, to increase by 1118 USD.

The regression with Control of Corruption as the independent variable produces the strongest results. The p-values are significant under both scenarios, though the R-squared is greater (71.6%) under the adjusted GDP per capita. Moreover, the coefficient for Control of Corruption is greater than that for Regulatory Quality, indicating that the former is a stronger predictor. It suggests that a 0.1 point improvement in the score of Control of Corruption, will cause an increase in GDP per capita$_t$ by 3243 USD, and an increase by 4326 USD in GDP per capita$_t$-1.

Lastly, Table 7 displays the results of the Full Model. The p-values for of the Full model is 0.000, indicating that the model

is statistically significant. The R-squared is fairly greater (75.9%) under adjusted GDP per capita (t-1). It also should be noted that the effect of Political Stability is statistically insignificant with both unadjusted and adjusted GDP per capita. The results of the Full Model indicate that, all other factors held constant, with a 0.1 point improvement in the score of Control of Corruption the GDP per capita for the same year that the indicator is based on (the year of data collection) is expected to increase by 3148 USD, while for the next year (the year when the score is published) it is expected to increase by 3795 USD.

CONCLUSION

Good governance is increasingly being advocated by international organizations, many public policy scholars and economists. It is widely believed to boost to the overall economic growth of a country as well as contribute to a more desired sustainable economic development. This paper examines the relationship between the Worldwide Governance Indicators developed by Kaufman et al (1999), and economic growth in Kazakhstan. The results show that good governance matters in Kazakhstan, too.

Based on the findings, the following recommendations can be suggested. First, the quality governance can strongly explain the economic growth of Kazakhstan; hence policymakers should pay attention to governance indicators in order to achieve higher economic growth. Second, the Control of Corruption has appeared to be the strongest predictor of economic growth in Kazakhstan's case. Thus, public administrators and the leadership of the government of Kazakhstan should prioritize fighting corruption in the public policy agenda, especially, given that there has been made only a marginal progress in this indicator by Kazakhstan.

There is a number of limitations to this study. First, there is relatively small

number of observations because only 19 years of available data is included in the analysis. Thus, it is suggested that this analysis is replicated annually in order to better understand the relationship. Secondly, reverse causality issue should be explored, since one might argue that there could have been another strong factor that caused economic growth of Kazakhstan (e.g. high oil prices), which then has led to better opportunities in improving the governance of Kazakhstan (e.g. Bolashak program). This could be a future research subject in order to better understand governance and its impact, in particular in Kazakhstan's case.

ACKNOWLEDGEMENT

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