

# The Impact of Governance Indicators on Nigerian Economic Performance

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**ABSTRACT:** *This study investigated the impact of governance indicators on economic performance in Nigeria. The study used time series data spanning the period from 1996 to 2021. The governance indicators were operationalised by using the World bank database on governance indicators. In order to address endogeneity problem, the study employed generalised method of moments (GMM) technique to analyse the data. The results indicate that overall average governance, government effectiveness and control of corruption exert positive impact on economic performance, but not significant. While voice and accountability, and political stability have positive and significant impact at 5% and 10% level, respectively. In contrast rule of law negatively impacted on economic performance at 5% level of significant, while regulatory quality is negative, but not significant.*

**KEYWORDS:** *Economic performance, governance indicators, GMM, Nigeria.*

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## 1. Introduction

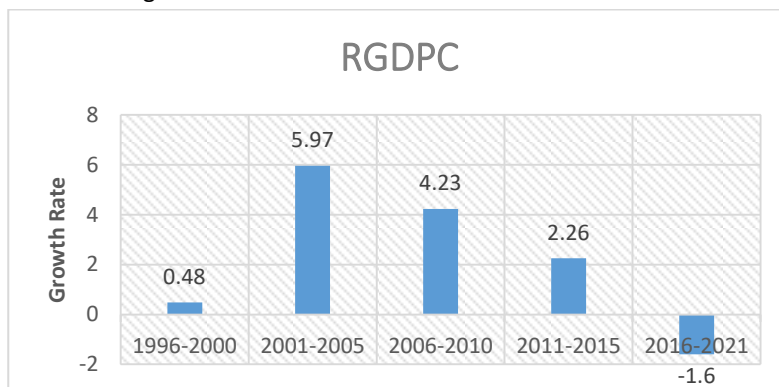
The importance of physical capital and human capital cannot be undermining in economic development; governance quality plays an equally important role in this regard. Good governance quality index increases economic incentives, minimise information asymmetry and the cost of transactions. These contribute to successful resource allocation and contribute to the efficient operation of markets. Consequently, this promotes more investment by domestic and international investors and increases the level of trust of current investors. In general, good governance quality creates an environment for efficient functioning of markets and thus lead to economic performance (Kaufmann, Kraay, & Zoido-Lobaton ,1999; Busse & Groizard, 2008; Khamfula, 2007). Institutional governance has been identified to account for the differences in economic performance across countries (North, 1990; Acemoglu, Johnson and Robinson, 2004; Acemoglu and Robinson, 2008).

As a result of the importance of good governance in economic growth and development process, different measures of governance have been provided by many organisations. The most popularly used measures of governances are those of World Bank's World Governance Indicators (WGIs). The World Governance Indicators measure six dimensions of governance quality, namely voice and accountability (VA), political stability and absence of violence (PS), government effectiveness (GE), regulatory quality(RQ), rule of law(RL) and control of corruption(CC) (Kaufmann, Kraay & Mastruzzi, 2011).

Lack of good governance in Nigeria is evidence in the WGI data which indicate negative scores for Nigeria in all the six governance indicators since 1996. In this regards, Iyoboyi and Pedro (2014) attributed ineffective policy

implementation on the prevalence of weak governance in developing countries such as Nigeria. According to Rothstein and Teorell (2008), good governance improves economic performance and promote impartiality in the enforcement of laws and policies, therefore enhancing the rules and processes necessary for growth and development. Nigeria's economic performance has been fluctuating over the years which may be due to poor governance which frustrate deliverance of essential services for a better economy (see Fig.1). Despite Nigeria's vast human and natural resources, numerous initiatives to revitalise the economy have met with dismal failure (World Bank, 2012).

In the empirical literature, there are conflicting results on the role of governance indicators and economic performance as can be observed from the reviewed literature in section two of this paper. Furthermore, most of the analyses are cross-country studies, with few studies exclusively on Nigeria. This study, therefore, intents to further re-examine the impact of each of the governance indicators on Nigerian economic performance as well as the composite of the six governance indicators.



**Figure 1:** Nigerian 5-year average real GDP per capita growth rate (1996-2021).

**Source:** Author's representation from World Bank, World Development Indicators, 2022.

Following the introduction, the rest of the paper is structured as follows: section two presents the review of related literature, and section three analyses the methodology. Sections four and five discuss the results and the conclusion of the study, respectively.

## 2. Literature Review

According to the work of Huther & Shah (1996) governance is described as all areas of authority exercised by formal and informal institutions in managing a state's resource endowment. Following the same direction, Kaufmann et al., 1999 (KKZ,1999) and Kaufmann, Kraay, & Mastruzzi (KKM ,2003) describe governance as “the traditions and institutions that regulate the exercise of authority in a nation” which led to the establishment of the most widely used set of governance indicators to measure institutions (Zhuang, Dios & Lagman-Martin, 2010). From the references above, institutions and governances are two synonymous concepts that address the same issue and are used interchangeably and synonymously in literature (Zhuang, et al., 2010).

There is a vast body of literature on the effect of governance indicators on economic performance in both developed and developing countries. Most of these studies were cross-country analysis, providing evidence of both positive and negative impact of the various measures of the institutional quality on economic performance. Studies carried out by Mehanna, Yazbeck and Saredidine (2010) used a panel data analysis to investigate the effect of governance quality on economic performance for 23 MENA countries within the years 1996-2005. The six governance indicators provided by the WGI dataset were used for the study. The study found out that all the institutional variables have a significant impact on the economic performance of these countries. Similarly, Siyakiya (2017) investigated the extent of governance quality measures on economic performance in twenty-eight European Union and eight prospects to the Union from 1996-2014. The study applied the SGMM estimator and used both composite institutional variables and individual measures of the governance quality. The empirical results revealed significant positive relationship between institutional index and economic performance of the 36 countries. Furthermore, in the disaggregated institutional analysis, government effectiveness and voice and accountability are positively related to economic performance,

control of corruption and political stability are negatively related, while regulation quality and rule of law are insignificant. Kebede and Takyii (2017) appraised the connection between government effectiveness and regulatory quality on economic performance of twenty-seven African countries, using panel data covering the period from 1996-2014. The result from system generalized method of moments (SGMM) established positive relationship between the governance indicators and economic performance, as well as long-run relationship. Glawe and Wagner (2019) also provide evidence of positive effect of governance indicators on economic performance of thirty-five European countries during the period 1996-2014. The study showed that political stability, rule of law, regulatory quality, control of corruption and the average measures of the six indicators were more positive and significant in influencing economic performance in the selected sample. Atinafu (2019) analysed the casual linkage between governance indicators on real GDP per capita of twenty-seven African countries from 1996-2016, using both aggregated and disaggregated measures of governance indicators from WGI. The SGMM results documented positive and significant relationship between governance indicators (aggregated and disaggregated) and economic performance in the sampled countries. The results of the casual relationship show that quality of governance improve economic performance and vice versa. In Tanzania, Gibogwe, Nigo and Kufuor (2022) also reported positive relationship between the average measures of the six governance indicators and the GDP per capita growth rate covering the period between 1990 and 2021. Some studies have provided mixed effect of the measures of the governance indicators. For instance, Kilishi, Mobolaji, Yaru and Yakubu (2013) employed a SGMM estimator to determine the effect of governance quality on the real GDP per capita of thirty-eight Sub-Saharan African countries between 1996 and 2010. The study utilised all six governance measures provided by WGIs. The study reported that only the regulatory quality and rule of law among the institutional variables were significantly associated with GDP per capita. The study concluded that by improving the regulatory quality, the region's economic performance would be enhanced. Equally, Iheonu, Ihedimma and Onwuanaku (2017) examined the relationship between governance indicators and economic performance of twelve ECOWAS countries over the period 1996-2015. The study employed fixed effect (FE), random effect (RE) and panel two-stage least squares (PTLS) estimation techniques, using the six governance variables sourced from the WGI dataset. The fixed and random effect model showed that all the governance indicators have a significant positive impact on the real GDP per capita of the selected countries in the study. However, the results of the panel two-stage least square estimator, accounting for endogeneity, only government effectiveness is significant. In the same vein, Jilenga and Helian (2017) utilised the six measures of governance quality from WGIs dataset to investigate the impact of institutions on real GDP per capita of five East African nations from 1996-2015. The empirical results indicated that political stability, government effectiveness, rule of law and control of corruption significantly affect the countries' economic performance. In contrast, regulatory quality and voice and accountability have an insignificant association with real GDP per capita. Similarly, Epharpha & Kombe (2018) applied FE, RE and GMM to determine the influence of governance quality on economic performance of forty-eight Sub-Saharan countries over the time spanning 1996-2016. The study revealed that political stability has the most impact on economic performance in these countries. Furthermore, the study observed that countries with better governance obtained higher rate of GDP per capita growth than countries with lesser quality of governance. In another by Seyingbo and Adeniyi (2018), using panel data covering the period from 1996-2013 to examine the nexus between the six governance indicators on economic performance of twenty-eight Sub-Saharan countries. The empirical finding reported conflicting results: political stability, regulatory quality, and voice and accountability exert positive relationship with economic performance, while control of corruption, rule of law and government effectiveness indicate negative relationship. Similar mixed results were obtained by the study conducted by Abayomi and Chidiebere (2021) in their comparative analysis of the impact of governance indicators on economic performance of Ghana and Nigeria between 1996 and 2019. The study used three governance indicators (control of corruption, government effectiveness and regulator quality) from WGI database. The results from ARDL revealed that only control of corruption promotes economic performance in Ghana, while in Nigeria only government effectiveness enhances economic performance.

Most recently, the few studies, exclusively on Nigeria, have been conducted on the relationship between governance indicators and economic performance, using the WGI database. For instance, Utile, Ijirsher and Sen (2021) employed ARDL to analyse the quality of governance on Nigerian economic performance over the period 2001-2019. The study utilised the composite of the six governance indicators of WGI. The empirical results establish a long run relationship and that governance index negatively and significantly related to economic performance in Nigeria for the period. However, Ogbebor (2021) reported positive and significant relationship between rule of law and Nigerian economic performance as well as between regulatory quality and economic performance between 2000 and 2019, using Error correction model (ECM).

From the literature survey above, the relationship between governance indicators and economic performance are inconclusive and most of the studies are cross-country analysis. Therefore, this study intent to contribute to the literature by further re-examine the governance-economic performance nexus, focusing on Nigeria.

### 3. Methodology

#### 3.1. Theoretical Framework

This study synthesized neoclassical and endogenous growth models. Neoclassical model of growth emphasised the important contribution of capital stock to economic performance of a nation. However, the model is modified in this study by the inclusion of human capital in line with Mankiw, Romer & Weil (1992), which specified economic performance as function of effective labour, physical capital and human capital. In implicit form equation (1) is specified as:

$$Y = f(AL, K, H) \quad (1)$$

Where Y is output level, AL is effective labour, K is physical capital and H is human capital.

Dividing equation (1) by AL, equation (2) is obtained as:

$$y = f(k, h) \quad (2)$$

where y is the per capita output, k physical capital per effective labour and h is the human capital per effective labour. k can further be split into domestic and foreign physical capital. Thus equation (3) is specified as:

$$y = f(k^f, k^d, h) \quad (3)$$

where  $k^f$  and  $k^d$  are foreign capital and domestic capital, respectively.

Since the objective of this study is to investigate the impact of governance indicators on economic performance, governance indicators are then introduced into equation (3). Equation (4) is specified as:

$$y = f(k^f, k^d, h, GI) \quad (4)$$

Where  $GI = f(CC, VA, RQ, RL, PS, GE)$

#### 3.2 Model Specification

The model specification for this study is based on the above theoretical framework and exposition of other studies. Therefore, the model is thus specified in explicit form as follows:

$$\text{LnGDPPC} = \beta_0 + \beta_1 \text{LnGDPPC}_{t-1} + \beta_2 \text{LnOPN}_t + \beta_3 \text{LnIVN}_t + \beta_4 \text{LnFDI}_t + \beta_5 \text{LnEXCH}_t + \beta_6 \text{LnGZ}_t + \beta_7 \text{LnHC}_t + \beta_8 \text{LnGI}_t + \mu_t \quad (5)$$

#### 3.3 Description of Variables and sources

LnGDPPC is the gross domestic product per capita as a proxy for economic performance (current LCU).  $\text{GDPPC}_{-1}$  is one year lagged of LnGDPPC. LnOPN is trade openness (addition of exports and imports as percentage of GDP). LnINV is the gross capital formation as percentage of GDP, proxy for domestic capital. LnFDI is the net foreign direct investment as percentage of GDP, proxy for foreign capital. LnEXCH is the official exchange rate (us dollar per Naira). LnGZ is the general government final consumption as percentage of GDP, proxy for government expenditure. LnHC is the gross rate of secondary school enrolment ratio, proxy for human capital. LnGI is the governance indicators provided by World Bank, Worldwide Governance Indicators. Each of the six governance indicators are introduced into equation (5) one after the other, as well as the average of the six variables. This is in order to analyse the separate effect of each on economic performance.  $\beta_0 - \beta_8$  are the parameters estimated.  $\mu$  is the error term. All the variables are in their natural logarithms to normalised the

data series. The negative scores of the governance indicators for Nigeria were first converted into new positive range from 0-100, using the formula: New index = country indicator value – minimum indicator value divided by maximum indicator value – minimum indicator value multiplied by 100 (Giang, 2017). The higher index indicating higher quality of governance.

### 3.4 Estimation Technique

This study conducted pre-estimation analyse using descriptive statistics and the unit root test, employing Augmented Dickey-Fuller (ADF). The Generalised method of moments (GMM) suggested by Hansen (1982) were used as the estimation technique to control for endogeneity as the lag of the dependent variable was specified as one of the explanatory variables. Also, take care of any incidence of heteroscedasticity and serial correlation (White, 1984; Newey & West, 1987). The process allows for the instrumentalisation of the explanatory variables with appropriate lag to prevent the instruments from correlating with the error term.

## 4. Results and Discussion

The presentation of the results starts with the preliminary analysis, which include the descriptive statistics of the data series and the stationary test, followed by the GMM estimates.

### 4.1 Preliminary Analysis.

The summary of the descriptive statistics of the data series are presented in Tables1a and Table1b. Tables1a and 1b show that all the data series are consistent as the mean and median values fall within the minimum and maximum values of the data series. The standard deviation of the series is generally low, the highest being 0.81(lnGZ) and the lowest is 0.05 (lnGI). Also, almost all the data series are normally distributed at 5% level of significance, except LnRQ, LnVA and LnEXCH.

Table 2 shows the results of the ADF unit root test. The results indicate mixture of order of integration. LnFDI, LnGE and LnVA are stationary at levels. While others are stationary at first difference.

**Table 1a: Descriptive Statistics for Institutional Variables**

	lnGI	lnGE	lnCC	lnPS	lnRL	lnRQ	lnVA
Mean	3.32	3.38	3.30	2.55	3.32	3.47	3.57
Median	3.32	3.38	3.29	2.48	3.31	3.49	3.58
Maximum	3.40	3.47	3.47	3.64	3.65	3.61	3.78
Minimum	3.20	3.25	3.06	1.79	3.06	3.14	2.94
Std. Dev.	0.05	0.06	0.09	0.39	0.15	0.11	0.17
Skewness	-0.25	-0.66	-0.78	0.75	0.21	-1.67	-1.95
Kurtosis	2.59	2.64	3.70	3.99	2.96	5.33	8.52
Jarque-Bera	0.46*	2.01*	3.18*	3.50*	0.19*	18.00	49.47
Probability	0.79	0.37	0.20	0.17	0.91	0.00	0.00
Sum	86.30	87.86	85.70	66.32	86.39	90.29	92.75
Sum Sq. Dev.	0.06	0.08	0.20	3.90	0.54	0.32	0.70
Observations	26	26	26	26	26	26	26

NB: \*Indicates normal distribution at a 5 percent level of significance

Source: Author's Computation (2023)

**Table 1b: Descriptive Statistics for Non-Institutional Variables**

	lnRGDP	lnOPN	lnINV	lnHC	lnGZ	lnFDI	lnEXCH
Mean	12.59	3.56	3.17	3.57	1.39	0.28	4.67
Median	12.67	3.63	3.27	3.55	1.66	0.46	4.61
Maximum	12.86	3.98	3.70	4.03	2.25	1.08	5.61
Minimum	12.22	2.79	2.70	3.16	-0.09	-0.69	4.24

Std. Dev.	0.23	0.31	0.34	0.25	0.81	0.54	0.35
Skewness	-0.52	-0.82	-0.03	-0.17	-0.74	-0.35	1.26
Kurtosis	1.72	3.04	1.63	1.96	2.04	1.93	4.30
Jarque-Bera	2.94*	2.90*	2.04*	1.29*	3.35*	1.79*	8.71
Probability	0.23	0.23	0.36	0.53	0.19	0.41	0.01
Sum	327.42	92.61	82.42	92.85	36.02	7.40	121.50
Sum Sq. Dev.	1.34	2.33	2.88	1.56	16.44	7.18	2.99
Observations	26	26	26	26	26	26	26

**NB:** \*Indicates normal distribution at a 5 percent level of significance

**Source:** Author's Computation (2023)

**Table 2:Result of Stationarity (Unit Root) Test**

Variable	ADF Statistic	1% Critical Values	5% Critical Values	10% Critical Values	I(d)	p-Value
InFDI	-1.977055	-2.66072	-1.95502	-1.60907	I(0)	0.0477
ΔInOPN	-6.019561	-3.737853	-2.991878	-2.635542	I(1)	0.0000
ΔInINV	-4.198864	-4.394309	-3.612199	-3.243079	I(1)	0.0151
ΔInGDPPC	-4.168949	-4.394309	-3.612199	-3.243079	I(1)	0.0161
ΔInEXCH	-5.214714	-3.737853	-2.991878	-2.635542	I(1)	0.0003
ΔInGZ	-5.496438	-3.737853	-2.991878	-2.635542	I(1)	0.0002
ΔInHC	-4.604232	-3.737853	-2.991878	-2.635542	I(1)	0.0013
ΔInCC	-5.565016	-2.664853	-1.955681	-1.608793	I(1)	0.0000
InGE	-4.23465	-3.72407	-2.986225	-2.632604	I(0)	0.0030
ΔInGI	-6.213247	-3.737853	-2.991878	-2.635542	I(1)	0.0000
ΔInPS	-5.137333	-3.752946	-2.998064	-2.638752	I(1)	0.0004
ΔInRL	-3.528432	-3.78803	-3.012363	-2.646119	I(1)	0.0174
ΔInRQ	-5.735759	-3.737853	-2.991878	-2.635542	I(1)	0.0001
InVA	6.104758	-3.72407	-2.986225	-2.632604	I(0)	0.0000

**Source:** Author's computation (2023).

#### 4.2 Finding and Discussion

Table 3 presents the GMM estimates of the impact of governance indicators on Nigerian economic performance for the period between 1996 and 2021. The impact of each of the six governance variables as well the overall average on economic performance were investigated. Therefore, seven models were estimated.

From Table 3, model 1 to 7 shows that the overall average governance indicator (InGI) has positive coefficient (0.261) and statistically insignificant (p-value 0.369) impact on economic performance; Government effectiveness (InGE) positive (0.327), but not significant (p-value 0.215); and control of corruption(InCC) also positive (0.266) and statistically insignificant (p-value 0.201). The implication is that governance generally, government effectiveness and control of corruption promote economic performance, but not substantially. Therefore, the need to improve them in order to make their impact significant. While voice and accountability (InVA) and political stability (InPS) have positive coefficients (1.215,0.1446, respectively) and statistically significant at 5%( p-value 0.032) and 10% (p-value 0.079), respectively. Furthermore, regulatory quality (InRQ) indicates negative coefficient (-0.025) and insignificant p-value, 0.836. while rule of law (InRL) also show negative coefficient (-0.684), but statistically significant at 5% level (p-value 0.026). this means that the regulatory quality and rule of law do not promote economic performance during the period under study.

It can be inferred that governance index, control of corruption, government effectiveness, voice and accountability, and political stability promote economic performance during the period of study, although governance index, control of corruption, and government effectiveness are not significant. While voice and accountability is significant at 5% level and political stability at 10% level of significant. In contrast, regulatory quality and rule of law do not promote economic performance. These results substantiate previous studies with conflicting outcomes on the impact of the measures of governance indicators on economic performance (Seyingbo and Adeniyi, 2018; Jilenga and Helian, 2017; Iheonu, et al., 2017; Kilishi, et al., 2013). Regarding the impact of other variables in the study on economic performance, gross domestic product per capita of the previous year (lnGDPPC(-1)), domestic investment (lnINV), government expenditure (lnGZ) and human capital (lnHC) significantly promote economic performance for the period under study.

**Table 3: Results of GMM Estimates**

Variable	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7
lnGDPPC(-1)	0.980*** (0.000)	0.783** (0.000)	0.981*** (0.000)	1.062*** (0.000)	1.013*** (0.000)	1.004*** (0.000)	0.988*** (0.000)
lnOPN	0.053 (0.552)	-0.074 (0.126)	0.033 (0.534)	0.125*** (0.007)	0.096 (0.161)	0.101 (0.239)	-0.065 (0.260)
lnINV	0.584*** (0.006)	0.675 (0.013)	0.437** (0.016)	0.342 (0.243)	0.451** (0.029)	0.491** (0.023)	0.321** (0.043)
lnFDI	0.021 (0.468)	0.157 (0.0194)	0.021 (0.358)	-0.033 (0.191)	-0.004 (0.902)	0.004 (0.919)	0.030* (0.091)
lnEXCH	-0.375* (0.09)	0.052 (0.752)	-0.291* (0.081)	0.195 (0.362)	0.086** (0.038)	-0.325 (0.213)	-0.557** (0.012)
lnGZ	0.041 (0.342)	0.146** (0.053)	0.032 (0.351)	0.073** (0.040)	0.664 (0.098)	0.052 (0.371)	0.065** (0.038)
lnHC	0.880*** (0.005)	1.109*** (0.009)	0.652** (0.015)	-0.070 (0.901)	0.145** (0.042)	0.647** (0.035)	0.552** (0.041)
lnGI	0.261 (0.369)	-----	-----	-----	-----	-----	-----
lnVA	-----	1.215** (0.032)	-----	-----	-----	-----	-----
lnRQ	-----	-----	-0.025 (0.836)	-----	-----	-----	-----
lnRL	-----	-----	-----	-0.684** (0.026)	-----	-----	-----
lnPS	-----	-----	-----	-----	0.1446* (0.079)	-----	-----
lnGE	-----	-----	-----	-----	-----	0.327 (0.215)	-----
lnCC	-----	-----	-----	-----	-----	-----	0.266 (0.201)
C	-4.036 (0.127)	-7.955** (0.034)	-2.115 (0.155)	-0.608 (0.797)	-2.672** (0.037)	-3.845* (0.055)	0.824 (0.623)
R-squared	0.991	0.993	0.994	0.993	0.992	0.992	0.993
Adj. R-squared	0.985	0.987	0.99	0.989	0.988	0.988	0.992
DW Stat.	2.31	2.67	2.52	1.99	2.31	2.32	2.61
Instr. rank	15	15	15	15	15	15	15

J-stat.	3.92	3.454	4.987	3.571	3.085	2.472	3.834
Prob(J-stat.)	0.69	0.75	0.55	0.73	0.798	0.87	0.699

**NB:** \*, \*\*, \*\*\* represents significance at 10%, 5 per cent and 1%, respectively. Probability of t-statistic is in the parenthesis.

**Source:** Author's Computation, 2023

## 5. Conclusion and Recommendations

In the literature, studies have been conducted on the impact of the various dimensions of governance indicators on economic performance in both developed and developing countries. The measures of governance provided by worldwide Governance Indicators are mostly used in the literature. There are six measures: control of corruption, voice and accountability, government effectiveness, regulatory quality, rule of law and political stability. Studies that have investigated the links between these measures of governance and economic performance provided conflicting results. Moreover, most of these studies are cross-country analysis. However, there are few studies focusing exclusively on Nigeria, therefore, this present study evaluates the impact of the six variables of governance indicators on Nigerian economic performance, using annual time series data from 1996-2021. The GMM results indicate that governance index, control of corruption, government effectiveness, voice and accountability, and political stability promote economic performance, although only voice and accountability, and political stability that are significant. While regulatory quality and rule of law have no impact on economic performance. This study affirms the mixed results from the literature regarding the effect of the various measures of governance quality on economic performance. The contradictory results could be attributed to the individual country's governance quality and the period of study.

The policy implication of this current study for Nigerian is that government should generally improve the quality of governance, if the country is desirous of **improving** the economic performance, which invariably would improve the quality of lives of average Nigerians.

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