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POLITICAL INSTITUTIONS AND MACROECONOMIC PERFORMANCE: AN EMPIRICAL ANALYSIS IN A SAMPLE OF MIDDLE-INCOME GROUP COUNTRIES[1]

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ABSTRACT

When the development journeys of countries are evaluated, it is observed that non-economic reasons are as important as economic variables. One of the studies that have attracted more and more attention in recent years is the examination of the institutional infrastructure that these countries have developed over the centuries while explaining the development or underdevelopment of countries. In this study, governance data prepared with the support of the World Bank is used as an indicator of institutionalisation. As indicators of economic performance, consumer price index, foreign direct investment and GDP per capita data are used. While choosing the data, annual data covering the period 2002-2021 and middle-income countries were preferred as the country group. According to the statistical results obtained, it is seen that institutionalisation indicators and macroeconomic indicators support each other. The most striking result was found between anti-corruption and macroeconomic indicators. Accordingly, economic variables are negatively affected by the fight against corruption. In other words, some countries should ignore the fight against corruption for a while in order to achieve economic growth.

Keywords: Institutional Economics, Political Economy, Economic Development

POLİTİK KURUMLAR VE MAKROEKONOMİK PERFORMANS İLİŞKİSİ: ORTA GELİR GRUBU ÜLKELER ÖRNEKLEMİNDE AMPİRİK BİR ANALİZ

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ÖZET

Ülkelerin gelişme serüvenleri değerlendirildiğinde iktisadi olan değişkenler kadar, doğrudan iktisadi olmayan nedenlerin de oldukça önemli olduğu göze çarpmaktadır. Son yıllarda gittikçe daha fazla dikkat çeken çalışmalardan birisi de ülkelerin gelişmişliğini veya geri kalmışlığını açıklarken, bu ülkelerin yüzyıllar içerisinde geliştirdiği kurumsal alt yapının incelenmesidir. Bu çalışmada kurumsallığın bir göstergesi olarak Dünya Bankası tarafından desteklenerek hazırlanan yönetişim verilerinden faydalanılmıştır. Ekonomik performansın göstergeleri olarak ise tüketici fiyat endeksi, doğrudan dış yatırımlar ve kişi başına düşen GSYH verileri kullanılmıştır. Veriler tercih edilirken 2002-2021 dönemini kapsayan yıllık veriler ve ülke grubu olarak orta gelir grubu ülkeler tercih edilmiştir. Elde edilen istatistiksel sonuçlara göre büyük orandan da kurumsallık göstergeleri ile makroekonomik göstergelerin birbirini desteklediği görülmektedir. En dikkat çekici sonuç ise yolsuzlukla mücadele ve makroekonomik göstergeler arasında tespit edilmiştir. Buna göre yolsuzlukla mücadele edildikçe, ekonomik değişkenler olumsuz etkilenmektedir. Başka bir deyişle bazı ülkeler ekonomik büyüme elde edebilmek için yolsuzlukla mücadeleyi bir süre göz ardı etmelidirler.

Anahtar Kelimeler: Kurumsal iktisat, Politik İktisat, İktisadi Gelişme

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INTRODUCTION

The search for "the ability of limited resources to meet unlimited needs", which is also included in the definition of economics, has been one of the main problems of all societies throughout history. In this context, in today's modern world, the interrelationships of social structure elements such as economics, state, politics, etc. are the main fields of endeavor of social sciences. In fact, one of the insoluble conflicts between various economic ideologies, and schools is the question of the "role of politics" and the "jurisdiction of the state" in economic life. A different interpretation contends that the interventionist role of the state and political influence will impair economic activities, despite the fact that some debates within this framework strongly support the idea.

Many research have been done recently to provide a scientific explanation of the interaction between politics and the economy. According to the common conclusion obtained from these studies, one of the most important conditions for the development of national economies and their sustainable growth performance is the existence of an environment of peace and confidence in the country. In societies where there is no environment of peace and trust, anomie, uncertainty, chaos, turmoil, despair and crises are expected and inevitable. In this context, ensuring an environment of social peace and trust is of great importance for the sustainable development, welfare, life and stability of countries. As a matter of fact, when the groups of developed and underdeveloped countries are analysed, it is seen that there is a significant relationship between political factors such as qualified democracy, political culture, political knowledge, awareness and interest and macro-economic indicators. On the other hand, it is not possible to establish a sustainable economic development in societies that have failed to establish the rule of law, have not internalised democracy and see politics as an activity carried out only to benefit from the blessings of power.

In this framework, we can summarise the reasons why the indicators that can constitute a source for macro-economic indicators are not at the desired level in two main points. The first, as mentioned above, is the situation where economic structures are influenced by political factors. In this case, economic structure components such as GDP per capita, unemployment rates, current account balance, inflation, production relations, consumption habits are frequently affected by policy changes. Likewise, in the event that political actors or politicians as a whole exhibit myopic behaviours and constantly change their policies or enact political economy programmes that are far from reality, the discipline of economics/economics is among the social structure units that will be directly affected by these conditions. In this sense, there is a direct relationship between the nature of the political process and macroeconomic assets.

Secondly, in the globalised world, there is a direct relationship between trade integration and macroeconomics. Today's modern world has turned into a "global village", as Mc Luhan put it. At this level, with the development of new communication technologies, especially social media, the concepts of time and space have disappeared; individuals, societies, institutions and states have become absolutely interrelated within a large network. The economic structures, legal rules, mass communication systems, education systems and other social structures of countries have become integrated with each other within the framework of international standards. In this context, in today's global world where labour, capital and information know almost no borders, sustainable economic structures are deeply affected not only by the dynamics of the country where they are located, but also by the international conjuncture. As a matter of fact, various political structure components such as the form of political administration, political stability, the functioning of the bureaucracy, the rule of law, the quality of democracy, and whether basic rights and freedoms such as life, liberty and property are secured in the country or countries with which the country is associated are of great importance for the economy.

A STRONG INSTITUTIONAL STRUCTURE, POLITICAL STABILITY AND ECONOMIC GOALS

Economic theories and many other social sciences are analysed using the "Ceteris paribus" approach. This means that all variables other than the variables whose effect is being investigated are constant. Although this approach is frequently used especially in theoretical approaches in economics, in real life all variables can change instantaneously and these changes can have an effect on each other. Theoretical economic models, which do not include all variables, may be insufficient to explain the events taking place in the whole economy with only the economic literature alone. For example, trying to explain macro-economic indicators such as growth, unemployment or inflation with only economics discipline may not be sufficient. Variables that are not used in the established models constitute the weakness of the relevant theory. However, in many economics studies conducted today, while analysing the functioning of the economy, other changes occurring at home and abroad are ignored in isolation.

Although economic developments are generally determined by factors of production such as labor, capital, natural resources, entrepreneurship, knowledge and technology in the most accepted form in the economic literature, other indirect determinants constitute the channels of economic growth, although their order of importance varies. Among the other determinants, the policy factor with a strong institutional structure and the related concepts of stability or instability come to the fore as an important factor in determining economic performance.

Today, the relationship between economics and politics can be seen in many country examples. Political instability and the resulting uncertainty lead to a decrease in investments and lack of economic growth. On the other hand, poor economic performance can lead to the fall of governments and political instability (Alesina et al., 1996:1). Therefore, economic stability and political stability are two complementary concepts. In other words, just as the most important component of political stability is economic stability, the most important component of economic stability is political stability.

Although the existence of a relationship between economy and politics is generally accepted, the extent of the relationship may vary according to countries. The relationship between politics and economy is realised more independently in countries with a developed institutional or legal structure than in underdeveloped countries. In developed countries, problems in the economy can be solved in a hurry in accordance with previously enacted laws. For example, problems such as unemployment, inflation and supply-demand imbalance can be solved with an update in interest rates. On the other hand, in undeveloped or developing countries, the solution of economic problems depends on the solution of many other problems. For this reason, many legal and institutional changes need to be realised by law. The debates, bickering or voting carried out by politicians who come together for this purpose can draw ordinary citizens into politics by finding an audience in the public in different ways. As a result, the discussions may lead to social losses by being perceived as a problem in society (Savaş, 2016:2).

On the other hand, in underdeveloped and developing countries, economic stabilization programs, which are not sustainable and depend on politicians, may be interrupted for some reasons. Since the financial markets in these countries are not sufficiently developed, the markets have not been integrated to the outside world and have not adapted to international competition, the stability programs implemented in these countries may require a longer period of time compared to other countries. Despite the length of time needed, stabilization programs are stretched due to frequent changes of power, elections and coups in undeveloped or underdeveloped countries. The governments, which tend towards populist policies in order to gain the support of the people, may move away from the medium-long term economic targets implemented by the country in order to realise their own political goals (Bulut, 2006:122).

In addition, underdeveloped and developing countries have a large savings deficit, high interest rates, capitalist and entrepreneur deficit. For this reason, it is almost impossible for the private sector to bring together the factors that will realise the investment. Therefore, many investments have to be realised by the state. Most of the time, these investments, which are vital for the needs and development of the country, may turn into an employment gate for political reasons or may be handed over to incompetent managers.

Politically appointed managers who rely on government support and power may bring a burden to the economy and cause deterioration of the public budget due to their inability to prepare the institutions they lead for the competitive-cost conditions of the age. Similarly, following populist policies during election periods and excessive recruitment of workers to public enterprises in order to reduce unemployment both reduce productivity and cause the emergence of hidden unemployment in the economy.

Politicians, like all other economic agents, act with the instinct to protect their own interests and maximise their benefits. The ultimate goal of politicians is to make themselves and their constituency successful in the next election. For this reason, many times they may not prefer decisions that may provide economic benefits in the long run for the sake of a short-term goal such as not losing votes in the next election. For example, during election periods when inflation tends to rise, they may harm the economy in the long run by implementing expansionary policies instead of implementing contractionary economic policies.

The direct relationship between economics and political sciences becomes clearer within the assumptions. Accordingly, the continuity of a sustainable successful economic performance can only be realised by ensuring a stable political climate. This can only be realised in systems where politicians are elected to power, political stability exists, the rule of law is accepted, the bureaucracy functions properly, internal and external conflicts are absent, moral values are respected and the individual is valued. As a result, it is often insufficient to explain the solution of economic problems in a society only with economic theories.

LITERATURE REVIEW

There has always been an interest in the ability of political institutions to influence other variables and as a result, various studies have been conducted on this topic. Studies evaluating the economic performance of nations usually include sub-headings that can be seen as measures of institutional quality such as rule of law, democratization, corruption and social violence. In this section, empirical and theoretical studies on the relationship between different political factors and economic variables are presented.

In his study, North (1991) stated that as institutions develop, the direction of economic change determines the direction of growth, stagnation or decline. According to Knack and Keefer (1995), institutions that protect property rights are crucial for economic growth and investment performance. According to Alesina and Perotti (1996), political instability caused by income inequality leads to a decrease in economic growth rates as a result of a decrease in investments. Feng (1997) found that economic factors are positively correlated with regular government change while they are negatively correlated with irregular government change. Goldsmith (1998) studied the effects of institutional deficiencies on the unfavourable course of the economy for Sub-Saharan Africa.

Grigorian and Martinez (2000) emphasised how judicial indicators and institutional quality have a positive impact on growth. According to Vijayaraghavan and Ward (2001), the two institutions that best account for variations in economic growth rates are the protection of property rights and the size of the government.

According to Acemoglu et al. (2003), weak institutional frameworks are responsible for changes in the macroeconomic structure of a country. Contrary to most other studies, Bloch and Glaeser et al. (2004) state that countries first get out of poverty and then improve institutions. According to Tang (2004), there is a significant correlation between high levels of technological progress and strong institutional structures and between high levels of technological progress and income levels. Rodrick (2004) emphasised that the quality of institutions is more important than many other variables. Klomp and Haan (2009) also find that political instability and policy uncertainty increase economic volatility. Alonso (2010) identifies the central role of institutions in economic growth. Vaal and Ebben (2011) find that the overall impact of corruption on economic growth depends to a large extent on the institutional structure of a country. They also argued that corruption can help economic growth when institutions are not well developed.

Brahim and Rachdi (2014) argue that strong institutions are necessary to achieve greater impact from foreign direct investment. Redek and Sušjan (2016) found that institutional quality is one of the factors contributing to economic performance. Haini (2020) found that institutional quality plays an important and positive role in economic growth. In developed countries, Ozdemir and Imamoglu (2021) discovered a causal link between growth and freedom of expression, effective governance, and high-quality regulations. On the other hand, it was discovered that there was no correlation between development and governance measures in developing nations throughout the full panel. Additionally, it is discovered that there is a causal connection between economic growth and governance indices when the facts of each individual country are examined.

DATA SET AND METHOD

In order to investigate the long and short-term effects of the data expressing political institutions and macroeconomic performance, an analysis was carried out for the years 2002-2021 for thirty-two countries, which are characterised as middle-income group according to the World Bank. Table 1 presents the definitions, abbreviations, country and period information for the variables subject to the study.

Consumer price index, GDP per capita and foreign direct investment data obtained from the World Bank database were utilised as dependent economic variables. As independent variables, the governance index created by Daniel Kaufmann and Aart Kraay was utilised. These variables are Voice and Accountability, Regulatory Quality, Government Effectiveness, Rule of Law, Political Stability and Absence of Violence/Terrorism and Control of Corruption.

Table 1: Definitions of Variables

Variables	Abbreviations	Countries	Period
Consumer price index (2010 = 100)	LCPI	Azerbaijan, Mexico, Guatemala, Sri Lanka, Botswana, Egypt, Guyana, Sudan, Brazil, Mongolia, Jamaica, Thailand, Bulgaria, Morocco, Kazakhstan, Tunisia, Dominican Republic, Nigeria, Colombia, Turkey, Equator, Paraguay, Costa Rica, Ukraine, Indonesia, Peru, Malaysia, Jordan, Armenia, Romania, Philippines, Russian Federation	2002-2021
GDP per capita (constant 2015 US$)	LGDP		
Foreign direct investment, net inflows (% of GDP)	LFDI		
Voice and Accountability	LVA		
Regulatory Quality	LRQ		
Government Effectiveness	LGE		
Rule of Law	LRL		
Political Stability and Absence of Violence/Terrorism	LPS		
Control of Corruption	LCC		

Panel data analysis, which offers both cross-sectional and time series features, was used in the study. Firstly, it is determined whether each series is horizontal cross-section dependent or not. Then, according to the results of the horizontal cross-section dependence test, the unit root tests to be used are selected. Finally, the model to be estimated as a result of the unit root properties of the series was selected and homogeneity test was performed for the model.

The selection of the unit root test to be applied to the series should take into account the horizontal cross-section dependence in panel data analysis. Neglecting horizontal cross-section dependence may lead to detrimental effects such as decreased estimator performance and unexplained residual dependence, which may invalidate test statistics. In this study, Breusch-Pagan (1980) LM, Bias-corrected scaled LM and Pesaran (2004) CD tests, which are widely used in the literature, are utilised.

In the study, the existence of a long-run relationship between the variables was investigated with Pedroni (1999, 2004) and Westerlund (2005) tests. The equations for testing the hypotheses claimed in the study are expressed as follows.

Hypothesis 1: There is a long-run relationship between inflation and governance variables.

Model 1: $\Delta LCPI_{it} = \gamma_1 + \beta_1 LVA_{it} + \beta_2 LRQ_{it} + \beta_3 LGE_{it} + \beta_4 LRL_{it} + \beta_5 LPS_{it} + \beta_6 LCC_{it} + \delta_1 LCPI_{it-1} + e_{it}$

Hypothesis *2: Hypothesis 2: There is a long-run relationship between GDP per capita and governance variables.*

Model 2: $\Delta LGDP_{it} = \gamma_1 + \beta_1 LVA_{it} + \beta_2 LRQ_{it} + \beta_3 LGE_{it} + \beta_4 LRL_{it} + \beta_5 LPS_{it} + \beta_6 LCC_{it} + \delta_1 LGDP_{it-1} + e_{it}$

Hypothesis 3: There is a long-run relationship between FDI and governance variables.

Model 2: $\Delta LFGI_{it} = \gamma_1 + \beta_1 LVA_{it} + \beta_2 LRQ_{it} + \beta_3 LGE_{it} + \beta_4 LRL_{it} + \beta_5 LPS_{it} + \beta_6 LCC_{it} + \delta_1 LFDI_{it-1} + e_{it}$

$$\hat{e}_{it} = \rho_i \hat{e}_{i,t-1} + \upsilon_{it} \quad (9)$$

Pedroni (1999, 2004) suggested seven heterogeneous panel cointegration tests. The average of the cointegration tests that were individually calculated for the time series of all units is used in the first of these tests. According to Yerdelen Tatoglu (2013), the limits of the piecewise numerator and denominator terms serve as the foundation for the limit distributions in the second category.

According to Westerlund (2005), the cointegration vectors for each panel have unique slope coefficients as illustrated in equation (9). By looking for a unit root in the residuals calculated using the DF regression in equation (9), VR test statistics are obtained. Based on a model where the AR value is either panel-specific or constant across all panels, Westerlund (2005) offered two possible test statistics. The alternative hypotheses that some panels are cointegrated in the panel-specific AR test statistic and that all panels are cointegrated in the same AR test statistic are tested against the null hypothesis, which states that there is no cointegration.

The long-run coefficients are calculated using the Pooled Mean Group (PMG) ARDL estimation method in this study. By enabling intercepts, short-run coefficients, and cointegration components to vary across cross-sections, the PMG model transforms the simple ARDL model's cointegration form to fit a panel setting. The PMG model can be expressed specifically using equation (12).

$$\Delta Y_{it} = \phi_i EC_{it} + \sum_{j=1}^{p-1} \lambda_{ij} \Delta Y_{it-j} + \sum_{j=0}^{q-1} \beta_{ij} \Delta X_{it-j}' + \varepsilon_{it} \quad (12)$$

$$EC_{it} = Y_{i,t-1} - X_{it}'\theta \quad (13)$$

The dependent variable and the regressors are both presumed to have the same number of lags in each cross-section in the PMG model. The regressors are also assumed to have the same number of lags in each cross-section for notational simplicity, while this assumption is not absolutely required for estimate.

In order to calculate the estimates of β_{ij} and λ_{ij}, Pesaran, Shin and Smith (1999) proposed an iterative procedure based on the first derivative of equation (13). Although the estimates of this iterative procedure are close to the full likelihood estimates, the covariance matrices do not converge. In contrast, the covariance matrix based on coefficient estimates constitutes an analytical form of estimation (Pesaran, Shin and Smith, 1999:625).

RESULTS

In this part of the study, the impact of governance variables, which refer to political institutions, on macroeconomic indicators for the period 2002-2021 for country groups is analysed through econometric tests and the findings are reported.

Table 2: Descriptive Statistics

	LCPI	LFDI	LGDP	LDIE	LDK	LHE	LHU	LPI	LY
Mean	4.662392	1.013593	8.475132	3.595966	3.796705	3.729452	3.576577	3.259634	3.480652
Median	4.673768	1.058871	8.522741	3.791774	3.940872	3.882753	3.721979	3.409831	3.668170
Maximum	9.695595	4.008657	9.498639	4.456750	4.336536	4.453444	4.284912	4.506079	4.444828
Minimum	3.596945	-2.870117	7.366482	0.901402	1.347074	1.450537	1.054595	-0.053541	-0.746688
Std. Dev.	0.473909	0.911638	0.503211	0.616138	0.508811	0.522549	0.544534	0.827773	0.686332
Skewness	2.990094	-0.301427	-0.096855	-1.626189	-2.245246	-1.947131	-1.381856	-1.185563	-1.969375
Kurtosis	28.72039	4.905775	2.103140	5.900289	8.838710	7.407426	5.138903	4.576512	9.832972
Jarque-Bera	18362.26	105.2124	22.16956	500.0606	1428.717	910.8879	321.6091	213.5010	1638.019
Probability	0.000000	0.000000	0.000015	0.000000	0.000000	0.000000	0.000000	0.000000	0.000000

Descriptive statistics of the series used in the study are presented in the table 2. The fact that the standard deviations of the series are not high indicates that the selected country groups are homogeneous. It is observed from Jarque-Bera statistics that all series are not normally distributed.

Firstly, horizontal cross-section dependence tests of the series were applied. Breusch-Pagan LM, Pesaran scaled LM, Bias-corrected scaled LM and Pesaran CD tests were used to test the horizontal cross-section dependence of the data. The results of the tests are shown in Table 3.

Table 3: Horizontal Cross-Section Dependence Tests

	LM_{BP}	LM_{PS}	LM_{BC}	LM_{CD}
LCPI	9266.379***	278.4598***	277.617***	96.18230***
LGDP	6621.885***	194.4970***	193.6549***	68.33686***
LFDI	1202.141***	22.41999***	21.57789***	13.18888***
LVA	2349.316***	58.84285***	58.00074***	3.219035***
LRQ	1782.871***	40.85820***	40.01609***	0.907954
LGE	1552.331***	33.53854***	32.69644***	-1.314250
LRL	1918.246***	45.15637***	44.31426***	6.416281***
LPS	2132.791***	51.96817***	51.12606***	3.998870***
LCC	1729.090***	39.15063***	38.30853***	-0.868355
*** denotes significance with a margin of error of 0.01.				

When the results of the four horizontal cross-section dependence tests for the series are evaluated, it is found that all series have horizontal cross-section dependence. (According to the LM_{CD} test, LRQ, LGE and LCC series are not horizontal cross-section dependent, but considering the results of the other three tests, it is accepted that these series have horizontal cross-section dependence). In this direction, Peseran (2007) CIPS tests, one of the second-generation unit root tests, were applied to the series and the findings obtained are emphasised in Table 4.

Table 4: Peseran - CIPS Unit Root Test

	Level		**First Dif.**	
	Constant	**Constant/Trend**	**Constant**	**Constant/Trend**
LCPI	-0.63812	-1.41791	2.75791***	-2.71191**
LGDP	-1.89355	-1.72976	-2.34883***	-2.68878**
LFDI	-1.47974	-2.95504**	-2.76139***	-3.35549***
LVA	-1.61512	-2.72634**	-3.48695***	-3.39815***
LRQ	-2.15337**	-2.34795	-3.67673***	-3.72448***
LGE	-2.72914***	-2.33469	-4.29344***	-3.70605***
LRL	-3.10096***	-3.08746***	-4.15731***	-4.36352***
LPS	-2.42941***	-2.22840	-3.96786***	-3.85993***
LCC	-1.69427	-2.34323	-3.91147***	-3.72893***
*** and ** denote significance at 0.01 and 0.05 error margin, respectively.				

Peseran (2007) CIPS results show that LCPI, LGDP and LCC series are stationary in their first differences. While LFDI and LVA series are stationary in level in the fixed-trend model, they are not stationary in level according to the fixed model. Similarly, LPS, LRQ and LGE series are stationary in level in the fixed model but not in level in the fixed-trend model. The LRL series is found to be stationary at level according to both models. When the findings of the unit root test are evaluated, considering that some of the series are I(0) and some of them are I(1), it is deemed appropriate to investigate the long-run relationship between the series with the PMG-ARDL test.

The slope heterogeneity test was applied for the models specified in Hypothesis 1, Hypothesis 2 and Hypothesis 3 and the delta test findings are presented in the Table 5.

Table 5: Slope Heterogeneity Test

	Model 1	**Model 2**	**Model 3**
$\hat{\Delta}$ Test	-1.237 (0.216)	0.497 (0.619)	-0.707 (0.480)
$\widehat{\Delta_{adj}}$ Test	-1.871 (0.061)	0.751 (0.453)	-1.053 (0.292)
$\hat{\Delta}$ Test (HAC)	-4.083 (0.000)	-1.716 (0.086)	-2.233 (0.026)
$\widehat{\Delta_{adj}}$ Test (HAC)	-6.173 (0.000)	-2.594 (0.009)	-3.328 (0.001)
Values in parentheses indicate probability values. To account for autocorrelation in the residuals, we use the Quadratic-Spehere kernel of Blomquist and Westerlund (2013) with HAC robust standard errors and a bandwidth of 15.			

According to the findings in the Table 5, according to the results of the delta test for all three models, the null hypothesis stating that "the slope coefficients are the same across cross-sectional units" cannot be rejected, which means that the panel is homogeneous. However, according to the delta HAC tests of Blomquist and Westerlund (2013), which take into account the autocorrelation in the residuals, the data for all three models are accepted as heterogeneous. The cointegration test results for the three hypotheses mentioned above are given in Table 5.

Table 6: Cointegration Tests

	Model 1		**Model 2**		**Model 3**	
	Statistic	**P-Value**	**Statistic**	**P-Value**	**Statistic**	**P-Value**
Kao Cointegration Test						
DF_t	1.1982	0.1154	-1.4972	0.0672	-5.0520	0.0000
DF_ρ	0.2837	0.3883	1.0834	0.1393	-3.4942	0.0002
DF_t^*	2.4692	0.0068	-1.4653	0.0714	-8.6512	0.0000
DF_ρ^*	2.4692	0.0006	1.1228	0.1308	-12.0685	0.0000
Pedroni Cointegration Test						
PP_t^*	8.5849	0.0000	7.4450	0.0000	5.4781	0.0000
PP_t	1.0751	0.1412	-0.3861	0.3497	-8.5130	0.0000
ADF_t	0.9197	0.1789	-0.0959	0.4618	-10.0173	0.0000
Westerlund Cointegration Test						
VR	20.3957	0.0000	12.2537	0.0000	1.0962	0.1365

When the cointegration test results for Model 1 are evaluated, according to the DF_t^*, DF_ρ^*, PP_t^* and VR tests, there is a cointegration relationship between the dependent and independent variables. According to the DF_ρ, DF_t^*, PP_t^* and VR tests of Model 2, the related variables are cointegrated in the long run. Finally, according to the test results for Model 3, all tests except the VR statistic indicate that the variables are cointegrated. The findings obtained from the Table 6 show that all three hypotheses are accepted.

In Model 1, the relationship between the CPI variable and the governance indicators expressing political institutions is analysed. In line with the theory and literature, an inverse relationship was found between the variables LRQ, LGE, LRL and LPS and the LCPI variable. Accordingly, a 1% increase in the Regulatory Quality (RQ) variable has a negative effect on inflation by 2.074891% and is statistically significant. Similarly, a 1% increase in Government Effectiveness (LGE) variable is expected to decrease inflation by 1.002455%, while a 1% increase in Political Stability and Absence of Violence/Terrorism (LPS) variable is expected to decrease inflation by 1.030870%. There is a negative relationship in the Rule of Law (LRL) variable, but the results are not statistically significant. There is a positive relationship between Voice and Accountability (LVA) and Control of Corruption (LCC) variables and inflation.

In Model 2, the relationship between GDP per capita (LGDP) and governance indicators is analysed. In line with the literature, an increase in LVA, LRQ, LGE and LPS variables increases GDP per capita and is statistically significant. An increase in LRL and LCC variables is found to decrease GDP per capita and statistically significant results are obtained.

Table 7: PMG-ARDL Estimation Results

	Model 1 ARDL (3,1,1,1,1,1,1)		**Model 2 ARDL (3,1,1,1,1,1,1)**		**Model 3 ARDL (2,1,1,1,1,1,1)**	
	Coefficient	**t-Statistic**	**Coefficient**	**t-Statistic**	**Coefficient**	**t-Statistic**
LVA	2.022643***	14.55606	0.251222***	2.925035	0.240795	1.616319
LRQ	-2.074891***	-6.864989	0.729835***	8.714693	0.640658***	3.510516
LGE	-1.002455***	-5.573799	0.607404***	8.053225	0.087403	0.609339
LRL	-0.091450	-0.449479	-0.315694***	-4.314761	0.456186***	2.731484
LPS	-1.030870***	-16.75423	0.261053***	11.45264	-0.147355***	-2.851021
LCC	0.903048***	6.190863	-0.212442***	-5.936953	-0.157515**	-2.191707
EC_{-1}	-0.025702***	-3.212215	-0.062495**	-1.920385	-0.449928***	-3.899888
Δ(LVA)	-0.111969***	-3.242893	0.020944	0.483587	-0.550142	-0.743208
Δ(LRQ)	-0.015119	-0.623461	0.083466	1.418038	-0.045619	-0.125395
Δ(LGE)	0.024014	0.934899	0.003483	0.069235	0.028500	0.053343
Δ(LRL)	0.037006	1.615146	0.004981	0.105787	-0.387093	-0.467498
Δ(LPS)	0.013455	0.871791	-0.034808	-0.918186	-0.244103	-1.045711
Δ(CC)	-0.021996	-1.003228	0.010119	0.334313	-0.041671	-0.090333
C	0.290677***	3.702043	0.237863**	2.193392	-1.556284***	-3.742776

In Model 3, the relationship between Foreign direct investment, net inflows (LFDI) and governance indicators is analysed. It is observed that an increase in LRW and LRL variables has positive effects on LFDI and is statistically significant. LVA and LGE variables also have positive effects, but the results are not statistically significant. An increase in LPS and LCC variables decreases LFDI and this effect is statistically significant. The inverse relationship between LFDI and LPS variables can be explained by the concepts of profitability and risk. In cases of increased risk, international capital owners may turn to these countries in the hope of achieving higher profitability.

In all three models, the LCC variable did not yield the expected results contrary to the theory. These results support the conclusion of Vaal and Ebben (2011) that corruption can help the economy when institutions are not well developed.

CONCLUSION

When economic theories are discussed, it is noticeable that there are basically two approaches. The first of these is the classical economics approach, which finds the state's intervention in the economy unnecessary in a way that disrupts the market of perfect competitive market, and the teachings that largely support the liberal teachings that developed afterwards. The second approach consists of Keynesian economics and its successors, which find state intervention in the economy necessary and beneficial. Whatever the accepted approach of the period, the influence of the state and institutions is an undeniable fact. Current neoliberal policies have largely given the state the role of a quarterback or regulator. In this context, the importance of political institutions and corporate governance has increased.

When the results obtained from the study are evaluated, it is seen that all three hypotheses established in the study are generally accepted. Accordingly, it was found that there is a long-run relationship between political institutions and inflation, GDP per capita and FDI. On a variable basis, it is observed that Voice and Accountability variable increases inflation, GDP per capita and FDI. Regulatory Quality variable decreases inflation and increases GDP per capita and FDI. While Government Effectiveness decreases inflation, it is found to increase GDP per capita. Rule of law variable has been observed to increase foreign direct investments although it decreases GDP per capita. Political Stability and Absence of Violence/Terrorism variable decreases inflation and foreign direct investments while increasing inflation. Control of corruption variable is observed to increase inflation while decreasing GDP per capita and FDI.

The results of this study show that factors reflecting institutional quality have a significant and statistically significant effect on macroeconomic aggregates. In conclusion, countries that want to achieve high levels of sustainable economic growth, reduce unemployment and current account deficit, and attract more foreign investors should first ensure political and economic stability, support the rule of law, protect intellectual property rights, and be open and transparent.

The period, model and variables used in the study constitute the strength of the study. While in many other studies, an assessment is made on a single economic variable; in this study, different variables are included. In particular, the results obtained regarding corruption contribute to the literature by claiming the contrary to what is generally known.

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