



# THE RELATIONSHIP BETWEEN GOOD GOVERNANCE AND SUSTAINABLE ECONOMIC DEVELOPMENT: THE CASE OF ALBANIA

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## **Abstract**

*Good governance is an important determinant for sustainable economic development in the country. The quality of government and its impact on economic growth has become more important in recent years, especially in transition countries such as our country that need to reform their institutions to meet the conditions for EU membership. After the 1990s, our country has undertaken and implemented a series of structural and institutional reforms in the direction of good governance. These reforms have aimed at increasing the effectiveness of the government, the performance of the public administration, and the best functioning of the public institutions. Some of the issues and challenges that must be addressed for good governance in our country are, drafting and implementation of sound legal and institutional policies; law*

*enforcement; macroeconomic stability; quality of public services, efficient use of public resources, transparency and accountability of public institutions. Good governance is an important instrument for the promotion of sustainable economic development, ensuring a fair and efficient management of human, capital and financial resources in the country. The purpose of this study is to examine the impact of good governance on economic development and growth in Albania. In this context, the six Worldwide Governance Indicators (WGIs) have been examined, respectively: Voice and Accountability, Political Stability and Absence of Violence, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption, during the period 2000 - 2022. The methodology used for this paper includes the collection and analysis of data regarding the main macroeconomic indicators; (GDP, GDP per capita, GDP growth, inflation, unemployment, and FDI) as well as indicators that evaluate the quality of good governance. The results show that there is a significant relationship between good governance and sustainable economic development in the country.*

*Keywords: Sustainable economic development, Good governance, Indicators, Relationship, Impact*

## **INTRODUCTION**

Sustainable economic development is one of the main goals that must be achieved in developing countries. Good governance is an important instrument for stimulating sustainable development in the country. According to the World Bank, good governance is evaluated by the implementation capacity of governance principles of a country, providing a framework for development and economic growth. It includes the processes of selecting, monitoring and replacing governments, as well as the government's capacity to formulate and implement policies effectively and sustainably.

In the World Bank report, (1994), the need for good governance was emphasized and identified as the existence of transparent processes, a government that takes responsibility for its actions, and a strong civil society engaged in public affairs acting under the rule of law. Good governance contributes positively to economic development, through the provision of supporting strategies and policies for economic growth, promotion and encouragement of the private sector, efficient use of public resources, and macroeconomic stability through sustainable fiscal policies.

The challenges addressed for good governance in Albania, are the rule of law, macroeconomic stability, economic growth, efficient use of public resources, citizens' well-being and transparency and accountability of public institutions.

In the long term, the policies of developing countries aim to achieve high levels of development in many of its dimensions. At the institutional level, states are governed by groups of elected officials and appointed administrators. Credibility and managerial capacity are two attributes that should characterize the leadership of an organization in the public sector. Monitoring the performance of public institutions, continuity and the will to implement reforms, the involvement of citizens and civil society in decision-making, control over corruption, and the implementation of the law, are elements that show that the governance of a country plays an important role in economic development of the country.

The implementation of good governance policies can promote economic development. There is a positive relationship between the quality of public institutions and economic growth. (Kaufmann & Kraay, 2002). Good governance requires an open and developmental policy, a professional administration, decision-makers who are willing to act for the public good and a strong civil society. In this regard, developing countries must focus more on reforms that improve governance if they want to achieve sustainable development. This concept includes the ability of the authorities to adequately identify and implement effective policies and procedures in selecting, monitoring and changing the governments, alongside respect for state and citizens for economic and community interaction institutions. Therefore, good governance in this paper refers to the processes and behaviours that serve decision-making and the exercise of power in a country, which is accessible and understandable to the general public, transparent, effective, coherent, easy to understand and ensures broad participation of citizens in it the entire set of decision-making policies.

Good governance promotes transparency, accountability, efficiency and the rule of law at all levels of public institutions. The implementation of good governance policies in Albania can promote economic development and ensure convergence towards the level of developed economies.

According to OECD (2020), good governance is critical to long-term economic, social and environmental development. The ability of governments to operate effectively and efficiently depends in part on their management policies and practices. It can be explained as participation, transparency and accountability, effective, equity promoting rule of law.

The purpose of this paper is to evaluate the relationship between governance and sustainable economic development in Albania. This goal will be fulfilled through some specific objectives, which are: 1) What relationship exists between governance and economic development in Albania? 2) To examine the indicators that have an impact on good governance, 3) To evaluate the impact of governance on economic growth and citizens' well-being.

The paper is designed as follows: In section 2, presents the theoretical background and literature review. In section 3, we introduce the research methodology. Section 4 presents, discussions and empirical results. In the last section, we present conclusions and recommendations.

## LITERATURE REVIEW

The quality of government and its impact on economic development has become more important in recent years, especially in transition countries such as our country that need to reform their institutions to meet the conditions for EU membership. Governance is considered a very important component of economic growth and the well-being of the citizens of a country. In this regard, the impact of governance, the quality of public administration, on economic development has been investigated theoretically and empirically in many studies.

This concept has many definitions provided by academics, researchers and policymakers. After the 1990s, considerable literature has empirically examined the impact of governance on economic growth and development, particularly by analyzing governance indicators.

The World Bank, (1994), defined governance as “how power is exercised in the management of a country’s economic and social resources for development”. This concept includes the ability of the authorities to adequately identify and implement effective policies and procedures in selecting, monitoring and changing the governments, alongside respect for state and citizens for economic and community interaction institutions. Since 1996, the World Bank has published six indicators measuring governance in different countries as part of the governance indicators project, namely the Worldwide Governance Indicators (WGI). Governance is defined as the process of the selection, monitoring and replacement of governments, the power of the government to effectively establish and perform sound policies; and the respect of citizens and the state for the institutions that govern economic and social interactions among them (Kaufmann, et al., 2010).

Good governance is, among other things, transparent and accountable, effective and equitable, and promotes and ensures the rule of law. It ensures that political, social and economic priorities are based on broad consensus in society and the participation of citizens in decision-making. Good governance can be defined as governance that has the practical effect of producing good outcomes for the public. (Elisa & Sara, 2011), their study examined the effect of good governance on economic growth and found that governance positively affects economic growth for both developing and developed countries. Raczkowska, et al. (2023), in their study,

confirm that there is a significant relationship between good governance and economic growth in EU countries.

According, to Mira & Hammadache (2017), good governance is the capacity of management and institutional reforms conducted by state policy that improves coordination and delivery of effective public services, and accountability of political actors and individual citizens in the driving of development policies. Since 1996, the World Bank has published six indicators measuring governance for more than 200 countries around the world namely the Worldwide Governance Indicators (WGI). Kaufmann et al. (2010) have developed these six indicators (WGI), corresponding to basic governance concepts, which, according to their study, show a strong causal relationship between good governance and improved development economic. Good governance in public institutions is the key to successful and satisfactory efficiency to achieve better performance. Through the analysis of the World Governance Indicators (WGI), most studies have concluded that good governance has a positive impact on growth and economic development.

Bayar (2016), argues that all public governance indicators except regulatory quality had a statistically positive impact on economic growth. Countries with better public governance use public expenditures more effectively, which positively affects economic growth. Samarasinghe (2018), referring to the analysis of the individual impact of World Governance Indicators, finds that corruption control plays a major role in the development of a country's economy. Fawaz et al. (2021), categorized a sample of 11 developing nations from 1996 to 2008 according to income levels. They also concluded that the rule of law and corruption control significantly impacted economic development. AlBassam (2013), investigated the relationship between governance and economic growth during times of crisis and found the existence of a significant, positive correlation between each governance indicator and gross domestic product (GDP).

Tarek & Ahmed (2013), argue that the institutional failure that characterizes developing countries inevitably leads to the destabilization of their long-term economic growth and an improvement in governance would greatly contribute to their economic growth. In developing countries, public governance has the potential to affect economic growth through many direct and indirect instruments because it is the main determinant of the economic environment and institutions that have a significant impact on the decision-making process of key economic actors. Acemoglu & Robinson (2010), consider public institutions as a key factor of economic growth. Government institutions can stimulate or reduce economic growth and development.

The development of the role of public administration has led to the decentralization of public services to allow better access for citizens to the services provided by the government. In our country, important reforms in the economic infrastructure sectors have been undertaken in

the last two decades, to improve the performance of service delivery to citizens by the government (Tomorri & Keco, 2023). Better governance also has the potential to positively affect economic growth by contributing to the development of domestic financial sectors and attracting more foreign direct investment. Kambo & Boshnjaku (2023), argue that to promote sustainable development in the country, the government should prioritize policies that promote sustainable economic growth and protect the environment.

Good governance of a nation results in a strong economic performance, and for a particular nation to effectively achieve its economic growth, the government has to explore the factors that can either reduce or increase the economic growth of a country. Governments worldwide are still seeking solutions that support sustainable development, and good governance is identified as a crucial tool for achieving this goal (Güney, 2017). In the long term, economic growth could be positively or negatively affected by government policy (Al-Naser & Hamdan, 2021). The efforts of international institutions and public authorities on sustainable development can also support the process of reducing poverty and increasing the well-being of the population, in developing countries (Mansi, et al. 2020).

Beleiu, et al. (2015), analyzed the impact of governance on economic growth and found a highly positive correlation, between the rule of law, regulatory quality and economic growth. Government or policymakers should widen their focus to include political and economic variables that affect economic growth. They should make every effort to achieve good governance and enhance economic growth (Mahran, 2023). The quality of governance has gained importance in recent years, both in developed and developing countries, as a way to promote effective and sustainable development. Petreski (2014), examined the impact of institutional quality on economic growth in transition economies and concluded that regulatory environments with good governance had a positive impact on economic growth. The results show that there is a strong positive relationship between the quality of governance and per capita income (Khyareh & Amini, 2021).

The focus of our study is examining the relationship between governance and economic development in Albania, which is based on the analysis of six WGI indicators, for the period 2000-2022.

## **MATERIALS AND METHODS**

Good governance is an important instrument for promotion and economic development in developed countries and especially in developing countries. The literature reviewed above reveals essential aspects regarding the relationship between governance and economic development, using multiple statistical methodologies. Based on the purpose and objectives of

this study, regarding the evaluation of the role of good governance on economic development in Albania, the examination of indicators that have an impact on good governance, as well as the impact of governance on economic growth and the well-being of citizens, we have used a descriptive and analytical approach about the purpose of the study.

The methodology used for this paper includes, the review of the literature related to the purpose of the study, collection of data published by national and international institutions as well as the analysis of data related to the indicators that evaluate the quality of good governance. The study is based on the use of the analysis method, through the collection, processing and interpretation of data and statistical indicators, focusing on the role and relationship between governance and the economic development of the country.

Table 1. The characteristics of good governance

<b>Characteristics</b>	<b>Description</b>
<b>Transparency</b>	Processes, institutions and information are directly accessible to all actors and citizens by providing sufficient information.
<b>Participation</b>	Involvement of citizens, stakeholders and government agencies in policy-making and decision-making processes.
<b>Accountability</b>	Responsibility of government institutions and organizations to citizens for their decisions and activities.
<b>Rule of law</b>	Drafting policies and implementing the activities of government organizations and institutions in compliance with laws and regulations.
<b>Effectiveness and efficiency</b>	The activity and competencies of government organizations in performing their functions and providing public services with efficiency and effectiveness.
<b>Responsibility</b>	Accountability in the provision of services and exchange of information by organizations, government institutions to citizens and other actors.

*Source: Authors' composition*

The six World Governance Indicators have been published since 1996 by the World Bank, are defined as follows:

- 1) "Voice and accountability": Reflects 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.
- 2) "Political Stability and Absence of Violence/Terrorism": measures perceptions of the likelihood of political instability and/or politically-motivated violence, including terrorism.
- 3) "Government effectiveness": Reflects 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.

- 4) “Regulatory Quality”: Reflects perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development.
- 5) “Rule of Law”: Reflects 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.
- 6) “Control of corruption”: Reflects 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.

The indicators used in the statistical analysis, their symbols and data sources are presented in Table 1.

Table 2: Indicators used in the statistical analysis

Indicators	Symbol	Unit of measure	Source
<b>GDP growth (annual %)</b>	GDP	(in %)	World Bank Indicators, 2023
<b>Voice and Accountability</b>	VA	(-2.5 to +2.5)	World Bank Indicators, 2023
<b>Political Stability and Absence of Violence</b>	PSAV	(-2.5 to +2.5)	World Bank Indicators, 2023
<b>Government Effectiveness</b>	GE	(-2.5 to +2.5)	World Bank Indicators, 2023
<b>Regulatory Quality</b>	RQ	(-2.5 to +2.5)	World Bank Indicators, 2023
<b>Rule of Law</b>	RL	(-2.5 to +2.5)	World Bank Indicators, 2023
<b>Control of Corruption</b>	CC	(-2.5 to +2.5)	World Bank Indicators, 2023

## RESULTS AND DISCUSSIONS

Considering the review of the literature and the methodology used, this paper focuses on the relationship and impact that governance has on the economic development of the country. In addition to the role of governance, other important factors that have determined the success of the reforms are related to the design and implementation of the legal and institutional framework. Albania faces important challenges such as the implementation of structural and



institutional reforms, the rule of law, economic growth, citizens' well-being, as well as the future integration into the European Union. During the last decade in Albania, significant positive developments have been observed in the quality and variety of public services offered through the e-Albania platform, showing the government's efforts to improve the quality of public services for citizens.

Some of the issues and challenges that must be addressed for good governance in our country are, drafting and implementation of sound legal and institutional policies; law enforcement; macroeconomic stability; quality of public services, efficient use of public resources, transparency and accountability of public institutions. The results show that there is a long-term relationship between government quality and economic growth for indicators analysed; government effectiveness, voice and accountability, political stability and absence of violence, regulatory quality, rule of law and control of corruption.

Referring to the data of the World Bank, we will analyze below the main macroeconomic indicators in Albania.

Table 3: The main macroeconomic indicators in Albania

Indicators	GDP/ mln \$	GDP per capita/ \$	GDP growth (annual %)	Inflation in %	Unemployment in %	Foreign direct investment in % of GDP
2000	3,632	1,176	6.67	0.05	14.15	3.94
2002	4,435	1,454	4.23	7.77	14.85	3.04
2004	7,315	2,417	5.71	2.28	13.91	4.67
2006	8,993	3,005	5.43	2.37	13.06	3.62
2008	12,881	4,371	7.53	3.36	13.00	9.63
2010	11,927	4,094	3.71	3.55	14.20	9.13
2012	12,320	4,248	1.42	2.03	13.44	7.47
2014	13,220	4,569	1.80	1.63	17.49	8.69
2016	11,864	4,125	3.37	1.28	15.22	8.80
2018	15,103	5,269	4.15	2.03	13.90	7.97
2020	15,132	5,343	-3.30	1.62	13.07	7.06
2022	18,882	6,803	4.84	6.73	11.81	7.63

Source: World Bank, 2023

According to the above data, it turns out that the Gross Domestic Product (GDP) for the year 2000 was 3,632 mln \$ and for 2022 it is 18,882 mln \$.

The Gross Domestic Product per capita, it turns out that in 2000 it was 1,176 \$, while in 2022 it is 6,803 \$. Referring to the data for GDP growth (annual %), it turns out that in 2000 it was 6.67% and in 2022 it is 4.84%.

Referring to inflation data, it results in a decreasing trend from 2010 to 2020. In 2022, it is 6.73%, as a result of the increase in prices at the global level, affected by the Covid-19 pandemic and the war in Ukraine.

Referring to the unemployment rate it turns out that in 2000, it was 14.15% and in 2022, it is 11.81%, with a decreasing trend. As for foreign direct investments in % of the gross domestic product, for the year 2000, they were 3.94% and for 2022 they are 7.63%, with an increasing trend.

Researchers, policymakers, international institutions, etc., in recent years, have analyzed and examined the relationship and impact of good governance on the sustainable development of a country.

Based on the data of the World Bank, the quality of governance is evaluated with six governance indicators. The quality of Government Index is a summary of these sub-indicators. According to different theoretical perspectives and supported by empirical studies, good governance significantly affects the economic growth of a country. The ranking of the values of the indicators is done from the lowest to the highest, which means that the higher the value of the indicator, the more positively it affects the quality of governance. The quality of governance and public institutions significantly affects economic development and shows differences in economic growth between different countries.

The table below presents the values of six indicators that evaluate the quality of governance in Albania.

Table 4. Values of six governance indicators (WGI) for Albania, 2000-2022 period

Year	Voice and Accountability	Political Stability	Government Effectiveness	Regulatory Quality	Rule of Law	Control of Corruption
2000	-0.29	-0.54	-0.92	-0.42	-1.02	-0.86
2002	-0.01	-0.30	-0.62	-0.31	-0.76	-0.85
2004	0.01	-0.43	-0.41	-0.19	-0.70	-0.72
2006	0.08	-0.51	-0.58	-0.15	-0.70	-0.79
2008	0.17	-0.03	-0.37	0.14	-0.60	-0.61
2010	0.11	-0.19	-0.27	0.23	-0.44	-0.49
2012	0.01	-0.16	-0.27	0.20	-0.54	-0.70
2014	0.15	0.45	-0.07	0.23	-0.37	-0.55
2016	0.17	0.34	0.06	0.20	-0.30	-0.45
2018	0.18	0.37	0.11	0.27	-0.40	-0.52
2020	0.09	0.09	-0.12	0.24	-0.35	-0.55
2022	0.14	0.11	0.07	0.16	-0.17	-0.41

Source: World Bank, 2023

Referring to the data in Table 4, the values of these indicators are interpreted as follows.

- *Voice and Accountability*, has a positive trend and values after 2004 and continues until 2022. This indicator has improved, positively influencing the quality of governance.
- *Political Stability and Absence of Violence*. This indicator had negative values until 2012. From 2014 onwards, this indicator has positive values and a significant impact on the quality of governance, which indicates political stability in our country.
- *Government Effectiveness*. This indicator had negative values until 2014. While for the period 2016- 2022, there are positive values. The improving values of this indicator show the government's efforts to increase the quality of public services.
- *Regulatory Quality*, has a positive trend and values after 2008. This indicator has had a positive impact on the quality of governance, in terms of the drafting and implementation of sound policies and regulations that promote and support the development of the private sector.
- *Rule of Law and Control of Corruption*, are the two indicators that have negative values for the entire 2000-2022 period. This means that although the rules and laws are well drafted by the government, their implementation remains a problem. The rule of law and control of corruption continue to be one of the main challenges for our country.

*Based on the above data analysis, we conclude with some key findings:*

- Control of corruption and the rule of law are two indicators that negatively affect the quality of governance. Control of corruption shows that it has negatively affected the main determinants of economic growth, such as the effectiveness of the public sector, domestic and international investments, tax collection and public expenditure management.
- Rule of law has a great impact on the economic performance of our country. The rule of law is considered a key indicator of good governance, as it is important for maintaining public order and security, providing public goods and services, effectively controlling corruption, and promoting economic development.
- Government effectiveness reflects the quality of public services, government decision-making and civil servants. In our study, government effectiveness had a positive impact on economic growth, confirming these theoretical considerations.
- Voice and accountability and political stability, have a positive impact on the country's economic growth. When citizens of a country believe in government institutions and that they receive public services and sufficient income, then their willingness to contribute to their country increases. Moreover, freedom of expression, freedom of organization and a

free media contribute to economic growth by influencing the performance of public administration.

The quality of governance can affect economic development through the promotion of private investment and indirectly influence the level of economic growth. Good governance is of particular importance, especially in developing countries, because it significantly affects economic development and examines the differences in economic development between different countries.

Albania has made important steps towards the quality of governance. Political stability and the rule of law have a significant impact on the implementation of economic reforms to become a member of the European Union.

## CONCLUSIONS

This paper examined the relationship between governance and sustainable economic development in Albania. The quality of government and its impact on economic development has become more important in recent years, especially in transition countries such as our country that need to reform their institutions to meet the conditions for EU membership.

Developing countries, like our country, have experienced a long and difficult process of transformation from centralized economies to market economies. After the 1990s, Albania has undertaken and implemented substantial economic, political and institutional reforms in good governance. These reforms have aimed at increasing the effectiveness of the government, the performance of the public administration, and the best functioning of the public institutions.

Some of the challenges that must be addressed for good governance in Albania are; the drafting and implementation of legal and institutional policies; law enforcement; macroeconomic stability; quality of public services, efficient use of public resources, sustainable economic development, citizens' well-being, transparency and accountability of public institutions.

Good Governance is represented by six world governance indicators (WGIs) defined by the World Bank: voice and accountability, political stability and absence of violence, government effectiveness, regulatory quality, rule of law, and control of corruption.

The results show that there is a long-term relationship between the quality of governance and economic development in the country for the indicators analyzed in this study. Political stability and government effectiveness are crucial for sustainable development in Albania. The government must ensure the rule of law, to minimize corruption and increase the trust of citizens in public institutions.

Policymakers must formulate and implement sound policies and strategies that encourage and support private sector development which is essential for sustainable economic

growth. The performance of economic development in our country is closely related to macroeconomic and financial stability, the quality of governance, the rule of law, better management of public resources, and efficient use of natural resources.

Strengthening public institutions, increasing the performance of public administration, transparency and accountability, and participation of citizens in decision-making processes, are essential for good governance. The government must prioritize the implementation of policies and strategies that promote sustainable economic growth, reduce poverty and inequality, and increase citizens' well-being.

## LIMITATIONS AND FURTHER STUDIES

The research has its limitations, but the results and findings of the study are intended to help the government and relevant institutions, to improve and promote good governance in terms of activities and services provided.

Future studies shall aim at a more in-depth analysis of good governance, in terms of the formulation and implementation of sound policies and strategies, the rule of law, transparency, accountability, and better management of public resources, with a focus on growth and sustainable economic development in the country.

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