Trust, Freedom, Governance and Social Capital; a Cross Section Analysis

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Abstract: The aim of this paper is analyzing the effect of trust, freedom and governance on social capital based on a cross section analysis for 110 countries at 2010 year. Results indicate that trust, governance and freedom have a significantly positive effect on social capital. The effect of governance on social capital is more than other variables. So, governance is the very important key on social capital. According to this paper, policy makers should support political and social freedoms.

Key words: Trust, Freedom, Governance, Social Capital, Cross Section Analysis

INTRODUCTION

Social capital is defined by its function. It is not a single entity, but a variety of different entities having two characteristics in common: They all consist of some aspect of social structure, and they facilitate certain actions of individuals who are within the structure (Coleman 1990). There has been considerable and increasing interest in social capital theory in recent years.

Knack and Keefer (1997) present evidence that “social capital” matters for measurable economic performance, using indicators of trust and civic norms from the World Values Surveys for a sample of 29 market economies. Memberships in formal groups—Putnam’s measure of social capital—is not associated with trust or with improved economic performance. They found trust and civic norms are stronger in nations with higher and more equal incomes, with institutions that restrain predatory actions of chief executives, and with better-educated and ethnically homogeneous populations.

Knack (2002) analyzes the impact of various forms of “social capital” on governmental performance in the American states. He concludes that aspects of social capital that are conceptually identified with generalized reciprocity (such as social trust, volunteering, and census response) are associated with better governmental performance, as measured by ratings constructed by the Government Performance Project. In contrast, aspects of social capital identified with social connectedness (including activity in associations and informal socializing) are unrelated to governmental performance. These findings call into question the use of heterogeneous indexes of social capital that mix social connectedness indicators together with indicators of generalized trust and reciprocity.

Keele (2006) indicates that trust is an evaluation of politicians and their management of the economy and responds immediately to any changes in government performance. But trust also reflects the lessons learned in civic activity and feelings of personal misanthropy. While changes in social capital will not register an effect on trust immediately, the effect on trust is substantively important. He has used macro-level data, the analysis is designed to capture the overtime variation in both social capital and government performance and let them compete to explain the macro variation in trust. His empirical results demonstrate that both government performance and social capital matter, but that social capital appears to be the force which accounts for the decline in trust over the last forty years.

The modern emergence of social capital concept renewed the academic interest for an old debate in social science: the relationship between trust, social networks and the development of modern industrial society. Social Capital Theory gained importance through the integration of classical sociological theory with the description of an intangible form of capital. In this way the classical definition of capital has been overcome allowing researchers to tackle issues in a new manner (Ferragina (2010)).

In this paper, we have analyzed the effect of trust, freedom and governance on social capital. We have used a cross section analysis for 110 countries.

This paper organized by four sections. The next section is devoted to data description and model specification. Section 3 shows empirical results and in final section, we have concluded.

Data Description and Model Specification:

We have used data for trust index, Governance Sub-Index Scores, Education Sub-Index Scores and Personal Freedom Sub-Index Scores variables from the Legatum Prosperity Index website. The Legatum Prosperity Index is the world’s only global assessment of wealth and wellbeing; unlike other studies that rank

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countries by actual levels of wealth, life satisfaction or development, the Prosperity Index produces rankings based upon the very foundations of prosperity those factors that will help drive economic growth and produce happy citizens over the long term.

Also, we have used the WDI2010 database for the share of consumption expenditure in GDP. We used 110 countries consist of: Algeria, Argentina, Australia, Austria, Bangladesh, Belarus, Belgium, Belize, Bolivia, Botswana, Brazil, Bulgaria, Cambodia, Cameroon, Canada, Central African Republic, Chile, China, Colombia, Costa Rica, Croatia, Czech Republic, Denmark, Dominican Republic, Ecuador, Egypt, El Salvador, Estonia, Ethiopia, Finland, France, Germany, Ghana, Greece, Guatemala, Honduras, Hong Kong, Hungary, Iceland, India, Indonesia, Iran, Ireland, Italy, Jamaica, Japan, Jordan, Kazakhstan, Kenya, Kuwait, Latvia, Lebanon, Lithuania, Macedonia, Malaysia, Mali, Mexico, Moldova, Mongolia, Morocco, Mozambique, Namibia, Nepal, Netherlands, New Zealand, Nicaragua, Nigeria, Norway, Pakistan, Panama, Paraguay, Peru, Philippines, Poland, Portugal, Romania, Russia, Rwanda, Saudi Arabia, Senegal, Singapore, Slovakia, Slovenia, South Africa, South Korea, Spain, Sri Lanka, Sudan, Sweden, Switzerland, Syria, Taiwan, Tanzania, Thailand, Trinidad and Tobago, Tunisia, Turkey, Uganda, Ukraine, United Arab Emirates, United Kingdom, United States, Uruguay, Uzbekistan, Venezuela, Vietnam, Yemen, Zambia, Zimbabwe.

We have used a cross section regression model for considering the effect of trust and governance on social capital as following:

\[ SP_i = \delta_1 + \delta_2 G_i + \delta X_i + e_i \]  

Where \( SP_i \) is social capital index, \( G_i \) is Governance Sub-Index Scores, \( X_i \) is the vector of control variables as: trust index and Personal Freedom Sub-Index Scores. The sign of \( i \) is country symbol.

We used ordinary least square method for parameters estimation. Estimation is done by Eviews.6 software.

**Empirical Results:**

Table 1 indicates the estimation results. Results indicate that trust, governance and freedom have a significantly positive effect on social capital. The effect of governance on social capital is more than other variables. So, governance is the very important key on social capital.

Based on these findings, policy makers should encourage political and social freedoms. In other hand, trust is one of the most important ingredients for improving social capita. Trust has a wide range: Trust between people and government, trust between people and people, trust between NGO and government and other institutions.

Good governance in development studies is one of the most important keys for development process. In contrast, bad governance as Zimbabwe severely damaged development process.

Table 2 indicates the Harvey test for Heteroskedasticity test. Results indicate that null hypothesis of Homoskedasticity is not rejected at 5% confidence level.

Table 3 indicates the Ramsey Reset test for testing model specification error. Results indicate that model specification is specified correct.

Figure 1 indicates that model is stable. Figure 2 and 4 indicate that the model coefficients are stable. Finally, figure 3 indicates the actual, residual and fitted.

### Table 1. Estimation Results

<table>
<thead>
<tr>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>C(1)</td>
<td>-1.621455</td>
<td>0.229919</td>
<td>-7.052273</td>
</tr>
<tr>
<td>C(2)</td>
<td>0.068817</td>
<td>0.008607</td>
<td>7.763532</td>
</tr>
<tr>
<td>C(3)</td>
<td>0.188726</td>
<td>0.077427</td>
<td>2.437461</td>
</tr>
<tr>
<td>C(4)</td>
<td>0.266607</td>
<td>0.081405</td>
<td>3.275068</td>
</tr>
</tbody>
</table>

R-squared: 0.688410  
Adjusted R-squared: 0.679592  
S.E. of regression: 1.008186  
Log likelihood: -154.9427  
Prob(F-statistic): 0.000000
Table 2: Heteroskedasticity Test: Harvey

<table>
<thead>
<tr>
<th></th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>F-statistic</td>
<td>1.766074</td>
<td></td>
<td></td>
<td>0.1581</td>
</tr>
<tr>
<td>Obs*R-squared</td>
<td>5.236420</td>
<td></td>
<td></td>
<td>0.1553</td>
</tr>
<tr>
<td>Scaled explained SS</td>
<td>3.570583</td>
<td></td>
<td></td>
<td>0.3117</td>
</tr>
</tbody>
</table>

Test Equation:
Dependent Variable: LRESID2
Method: Least Squares
Date: 08/16/11 Time: 04:03
Sample: 110
Included observations: 110

Table 3: Ramsey RESET Test:

<table>
<thead>
<tr>
<th></th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>F-statistic</td>
<td>0.137222</td>
<td></td>
<td></td>
<td>0.8719</td>
</tr>
<tr>
<td>Log likelihood ratio</td>
<td>0.289896</td>
<td></td>
<td></td>
<td>0.8651</td>
</tr>
</tbody>
</table>

Test Equation:
Dependent Variable: SP
Method: Least Squares
Date: 08/16/11 Time: 04:05
Sample: 110
Included observations: 110
Fig. 1: CUSUM Plot for Stability Test

Fig. 2: Confidence Ellipse Test for Coefficients

Fig. 3: Actual, Residual and Fitted Plot
Conclusion:
There has been considerable and increasing interest in social capital theory in recent years. Social capital is a sociological concept, which refers to connections within and between social networks. In this paper, we have considered the effect of governance, trust and freedom index on social capital in 110 countries at 2010 year. Results indicate that trust, governance and freedom have a significantly positive effect on social capital. The effect of governance on social capital is more than other variables. So, governance is the very important key on social capital. Good governance in development studies is one of the most important keys for development process. In contrast, bad governance as Zimbabwe severely damaged development process. Based on these findings, policy makers should support political and social freedoms.

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