

INSTITUTIONAL DETERMINANTS OF TOURISM DEVELOPMENT: THE CASE OF DEVELOPING COUNTRIES

Betul Piskin

Istanbul University, Turkey
betulpiskin@istanbul.edu.tr

Abstract:

It is an undeniable fact that a decline in the tourism revenues especially liquidity flow provided from tourism, which has occurred as a result of the ongoing coronavirus pandemic, is an important reason for the economic recession that has been experienced all over the world. In such a framework, the determinants of the tourism sector development are brought on the agenda again. Besides the widespread determinants of the tourism development such as economic growth, climate conditions, geography, political and international relations, there are elements that contemporarily discussed to have a notable impact on the development of the sector; the institutions which are widely defined as the legal framework in which political and economic decisions are taken. In this framework, using the linear regression model with OLS estimators, for 81 developing countries, the study tests whether institutional quality has a statistically significant impact on tourism development which is measured with international tourism receipts. To measure institutional quality, the study employs firstly the governance variables which are political stability and rule of law, and HDI and trade openness, which are accepted to be strongly correlated with institutional structure as secondary institutional variables. The results indicate that trade openness, rule of law, and human development index have a positive effect on tourism receipts as expected, while political stability has no statistically significant impact on it. The paper concludes that progressive institutional quality has a positive influence on tourism development in developing countries.

Keywords: Tourism Development, Political Economy, Institutional Quality, OLS Estimation, Rule of Law, Political Stability

JEL Codes: C21, P16, Z32

1. INTRODUCTION

Tourism is a significant contributing economic activity for economic growth and development with its labor-incentive nature especially for the developing countries which have plenty of labor supply. It creates several kinds of employment opportunities for different groups of society. It advances exchange inflows and is important for the current account balance. On

the other hand, it encourages local economic activities and helps to development of these local areas. There are several other stimulating characteristics of tourism on economy and these characteristics make it crucial to ensure a well-functioning tourism sector and to sustain the development of this sector. When the share of tourism and travel activities in the world economy is examined, it is seen that tourism and travel had 10.3% of the world GDP in 2019 (WTTC, 2020). These notable functions and contribution of tourism have made it attractive to economic research and have directed scholars to investigate the elements which increase or decrease the activity of the tourism sector and its revenue. Several examined factors determine tourism development such as geography, macroeconomic development, demography, technological developments, tourism activities, legal regulations, political and international conditions, etc.

Institutions whose determining role in the economy brought on the agenda by the Institutional Economists who brought a new interpretation to how the economic system comes to equilibrium are one of the elements that determine the level of development in the tourism sector like other economic sectors and variables. In a general manner, they refer to the legal structure in which economic and political decisions are taken. They include several kinds of components such as rules, regulations, tradition, political system, and economic system. In economics terms, they are widely defined as the legal environment in which economic agents proceed with their economic activities. When the tourism sector has considered with its social and cultural dimensions, it is obvious that the sector is fragile to the changes that can occur in this kind of framework which determine the decisions, behaviors, and even traditions of the society.

In this study, it will be tried to explore empirically the impact of institutions that has serious effects on the general ongoing life, policy, and economy, on tourism development which has a significant role in economic growth and development, especially for developing countries. In this framework, after the illustration of the theoretical framework and literature review, the data and methodology that will be used in the study will be examined. Following the formation of the model which will test the suggested relationship, the empirical investigation will be carried out and the evidence will be evaluated. At the end of the paper, the results will be interpreted in the light of theory and literature.

2. THEORETICAL FRAMEWORK

The tourism industry has experienced significant progress especially with the advance in transportation opportunities, globalization, and the advent of communication and advertisement. The rising tourism activities both domestic and international, have enhanced the sector's share in countries' gross domestic products. The growing tourism sector has gained importance as an alternative income gate for countries, especially the ones, having not been industrialized and developed enough with its roles to improve income distribution facilities, sustaining employment, and supporting the balance of payment. What makes tourism that much advantageous and attractive for economic development is that it does not only raise income directly but also it has a snowball effect which works as a multiplier and generates income in indirect ways (Honey & Gilpin, 2009). According to the report of the World Travel & Tourism

Council (WTTC) in 2019, tourism and travel activities have contributed to the world GDP by 10% in 2018, and this rate has reached 10.3% in 2019. Moreover, they forecast that this rate will drive up by 12% for the next ten years (COMCEC, 2019).

This growing significance of the tourism sector in the economic activity has directed authorities to improve tourism activities and to do this make some regulations and incentives. The countries, having wished to have higher tourism revenues and take the advantage of their tourism values, have been looking for ways to stimulate tourism and travel facilities. Even though concrete ways such as advertisement, trade agreements, visa contracts, etc. are seen as the primary determinants of the tourism flows, some notional elements are embedded in the countries' tradition, politics, human rights, development, and culture. These embedded factors which determine the political, legal, and social environment for the economic activity and widely defined as rules of the game (North, 1990), are the institutions that differ from country to country, from culture to culture. Institutions, having been suggested as the components that fill the gaps which cause transaction costs and accordingly inefficiency in the markets, by Institutional Economists, are defined as collective action in the control of individual action by Commons (1934) who is one of the pioneers of the school. This control can be in the shape of expansion, liberation, or the restriction of individuals who are the agents of economic activity (Klein, 1993). In the Institutionalist theory, it is emphasized that economic growth and development are not affected only by the factors such as income level, employment, capital accumulation, or technology, it is also impacted by the level of institutional development of the states (Sabir, Rafique, & Abbas, 2019). Institutions, in a conventional manner, are thought to be the political and economic environment that is provided to the market actors. According to this conventional approach, the economic agents who have the intelligence will do maximize their profit in an economic circumstance in which their rights are protected by the rule of law, democracy, and contractual arrangements (Beck & Levine, 2005). The institutional quality, then, refers to the legal framework in which the rights of the individuals are protected, the political decision-making processes' reliability and democracy are guaranteed, and the elimination of corruption and other kinds of legal deteriorations.

From the tourism perspective, it is suggested that the continual development of the sector is strongly linked with the collection of the formal or informal regulations, routines, rules, and collective concepts embedded in the organizational structure of the political economy (Jiang, Zhuo, Zhang, & Gao, 2019; Hall & Taylor, 1996). Institutional quality affects tourism development through two channels. The first one is directly attracting tourists and make them choose the country to visit. A country will tend to be visited more if there is peace, stability, and safety are guaranteed. The accessibility of transportation, safety, crime, marketing campaigns, the international appearance, the human rights conditions, the general development of the country is traditionally accepted as linked with the performance of the tourism sector (Roxas & Chadee, 2013). The second channel, on the other hand, is entrepreneurship and its power to attract tourists. As the institutional quality gets higher, the entrepreneurs will have the encouragement to make more investment in the sector which will make appealing the country to foreign visitors. On the other hand, degradation in the institutional structure of a country in the form of corruption, political instability, violation of human rights, and weak law implementation, has the possibility to create adverse conclusions to both overall economic conditions and the tourism sector (Mushtaq, Thoker, & Bhat, 2020). Thus, like the expectation

that institutional quality stimulates economic well-being, it is widely accepted that tourism development is also affected by the institutional structure and encouraged as the institutional quality rises.

3. LITERATURE REVIEW

Since the subject of institutions (institutional quality) or in other terms ‘governance’ is a relatively new concept whose relationship with economic variables is tested, the studies which look for the institutional determinants of tourism development or demand are also currently dated. Even though there are several studies, having searched the other determinants of tourism development, institutional determinants of tourism development are a relatively less studied research area. When the literature is searched, it is seen that institutional quality is a promoting determinant of tourism development. For instance, Yap and Saha (2013) provided evidence that there is an adverse relationship between tourism sector performance and political instability. They have proved that political stability is an important factor to improve tourism development. On the other hand, they also have shown that terrorism and corruption have negative effects on tourism sector development in their study which tests the relationships via fixed effect panel data analysis for 139 countries.

On the other hand, Roxas and Chadee (2013) have shown that the formal institutional environment stimulates entrepreneurship, accordingly the performance of the tourism sector in the Philippines. Balli et al. (2016), in their study, having employed panel data analysis for 52 middle to low-income countries, have demonstrated that the tourists consider the quality of institutions, along with freedom and civil liberty indices, when they select a destination. Mushtaq et al. (2020) have held that the impact of trade openness and development level of the host country (proxied by HDI) is found to have a positive association with the tourism demand. They have found that institutional quality has a positive relationship with the international tourism demand of India in their study which investigates the relationship between institutional quality and tourism demand for INDIA. Chaisumpunsakul and Pholpirul (2018) have provided evidence that international tourism demand is positively correlated with the degree of trade openness through time series analysis. Detotto et al. (2021), in their study which searches for the impact of the Worldwide Governance Indicators (WGI) on the tourism industry, have shown that regulatory quality and government effectiveness have a significant effect on a country’s ability to generate tourism income, while corruption is problematic for tourism development.

4. DATA AND METHODOLOGY

The regression analysis employed in this study uses cross-country data for the year 2018 for 81 developing countries. First of all, to measure tourism development, international tourism receipts as US dollar have been taken from the World Bank World Development Indicators (WDI) database by considering the fact that the demand for a country’s tourism is highly correlated with its tourism sector development. In the context where tourism demand can be

measured by handling four components which are tourists, expenditure, travel duration, and distance (Baggio, 2018) , international tourism receipts have been chosen to represent the development level of countries' tourism sectors in the study. When it comes to the independent variables, a control variable, GDP, has been employed to eliminate the omitted variable problem. The institutional quality has been measured by Political Stability and Rule of Law which are two important indicators of World Governance Indicators. Rule of Law indicates the level of reliability and of the rules of society and the degree to comply with these rules, and the quality of property rights, contract enforcement, police, and courts. Political stability, on the other hand, represents the contingency of government to be destabilized or to be overthrown by unconstitutional ways (Kaufmann et al., 2010).

TABLE 1: Selected Measures and Abbreviations

Abbreviation	Variable	Indicator	Source
LITD	Tourism Development	International Tourism Receipts	WDI
LNGDP	Control Variable	Gross Domestic Product	WDI
LNTRADE	Trade Openness	Total Trade	WDI
PS	Political Stability	Political Stability	WGI
RL	Rule of Law	Rule of Law	WGI
LHDI	Human Development Index	Human Development	UNESCO

Besides the rule of law and political stability, total trade volume as of GDP, having been taken from WDI, has been employed to measure the trade openness of the countries. Even though it is not one of the governance indicators, because openness in the trade actions is an important point that is directly related to the institutional structure of those countries, its involvement has been seen as necessary to establish a well-working model.

Finally, Human Development Index has been included in the model due to its ability to ensure a broader scope of development by especially focusing on education, income, and longevity (Moshirian, 2008) which are also directly determined by the institutional quality of countries. The data belonging to the HDI has been taken from the UNESCO database.

The descriptive statistics belonging to the data used in the study are shown in Table 2 below.

TABLE 2: Descriptive Statistics

Variable	Observation	Mean	St. Deviation	Min.	Max.
ITD	81	6.20e+09	1.03e+10	2.00e+07	6.52e+10
GDP	81	3.90e+11	1.58e+12	1.46e+09	1.39e+13
TRADE	81	77.93118	34.50194	17.92676	208.3067
PS	81	-.3464763	0.7421356	-2.516502	1.041839
RL	81	-.3454652	0.5673123	-1.758796	1.089803
HDI	81	0.6992963	0.1179092	0.431	0.854

According to these statistics, the mean of the international tourism receipts of selected countries is 6.2 billion dollars while the mean of trade volume is 77%. When it comes to political stability and Rule of Law which are rated between -2 and 2, it is seen that their means are respectively, -0.346 and -0.345 which are almost the same. It is not surprising that these numbers are that much close because they are strongly related to governance indicators. Finally, when HDI is described statistically, it is seen that its mean is 69% while the minimum and maximum values are respectively 43% and 85%.

The model, having been established to test the mentioned relationship is:

$$\text{LNITD} = b_1 \text{LNNGDP} + b_2 \text{LNTRADE} + b_3 \text{PS} + b_4 \text{RL} + b_5 \text{LNHDI} + e$$

where LNITD is the logarithm of international tourism receipts, LNGDP is the logarithm of the GDP, LNHDI is the log of human development index and LNTRADE is the logarithm of the total trade volume. The variables of political stability and rule of law are not taken as logarithm since they have negative values. The analysis will predict the bs on the equation to determine the significance and the direction of the independent variables on the dependent variable. After the determination of the robustness of the model through diagnostics tests, the estimated coefficients will be interpreted.

5. EMPIRICAL RESULTS

Before running the model with OLS estimators, the diagnostics that search for the properties of the OLS estimators have been progressed, and the existence of heteroskedasticity, multicollinearity, and the omitted variable problems have been tested. According to Breusch-Pagan Heteroskedasticity Test results, having been presented at the bottom lines of Table 3, because the probability of the test statistic is higher than 0.05, the null hypothesis indicating constant variance cannot be rejected which means that the standard errors of the model do not suffer from a changing variance problem. On the other hand, to check the existence of multicollinearity between the variables, variance inflation factors of each variable have been computed and it has been detected that there is no multicollinearity because all VIF values are lower than ten. Finally, the omitted variable problem has been tested through the Ramsey Reset Test whose null hypothesis indicates the absence of the omitted variable, and it has been seen that the probability of the F statistic is higher than 0.05 which prevents us to reject the null hypothesis. Thus, it has been specified that the model is free from the omitted variable problem too.

Following the diagnostic tests and being sure that there is no problem with the model, the model has been run and the results of the OLS estimation are represented in Table 3 below. Before the interpretation of the coefficients and their significance, it should be noted that the values of R² and adjusted R² which are high enough also indicate that the model is robust and reliable.

TABLE 3: OLS Estimation Results and Diagnostics

Variable	LNGDP	LNTRADE	LNHDI	RL	PS	Constant
Coefficient	0.6750221* (9.36)	0.543911* (2.36)	1.358494* (2.09)	0.231073* (2.45)	-0.0829139 (-1.12)	1.266791 (1.29)
Probability	0.000	0.021	0.040	0.017	0.266	0.235

R² = 0.7632

Adjusted R² = 0.7474

F = 48.34 (0.0000)

Diagnostics

Test	Null Hypothesis	Test Statistics	Probability
Breusch-Pagan Test	H0: Constant Variance	2.17	0.1405
Ramsey Reset Test	H0: Model has no omitted variables	0.96	0.4144

VIF Values of Variables

PS: 2.00 LNGDP 1.91 RL:1.91 LNHDI: 1.79 LNTRADE: 1.39

NOTE: The numbers in parenthesis represent t values for each coefficient.

According to the results of the estimation, first of all, it is seen that the control variable LNGDP is statistically significant and has a positive effect on tourism development; a unit increase in the gross domestic products is causing an increase in international tourism receipts by 0,67. When we look at the coefficient of total trade volume, it is seen that the coefficient is statistically significant at 5% level and has a positive effect on tourism development. The trade volume had been employed to determine the impact of trade openness on tourism development and it has been detected that trade openness is positively correlated with tourism development. Besides, the coefficient of rule of law is also statistically significant at 5% level and is positively correlated with tourism development as expected. The coefficient of LNHDI which is 1.35 is also significant and is strongly effective in tourism development. On the other hand, there has not been a significant relationship between political stability and tourism development in simple OLS regression. The coefficient of Political stability which was expected to be negative is not statistically significant.

In summary, in OLS regression analysis, it has been detected that rule of law, human development level, and trade openness have a positive impact on tourism development, while political stability has no effect on it.

6. CONCLUSION

The increasing importance of institutional factors in the economy has stimulated the studies that analyze the effect of these factors on different sectors of the economy as well as the overall economic conditions. In the light of vast literature on institutional quality, the definition of the institutions, and their roles, this study has tried to determine the correlation of these factors with tourism development, which is also an essential sector for sustainable economic development, especially for the developing countries. For this purpose, the study has employed 81 developing countries and tested the mentioned relationship with the help of simple regression analysis. The study has demonstrated that as mentioned in the literature, the institutions have an important effect on tourism development. According to the results of the simple regression model, it can be said that as the countries have institutions that provide the reliability of rules, property rights, human development, and accessibility of trade; they are expected to attract tourists and have higher revenues from the tourism sector.

REFERENCES

- Baggio, R. (2018). Measuring Tourism: Methods, Indicators, and Needs ., In C. a.-S. Cooper, *The Future of Tourism: Innovation and Sustainability* (pp. 255-269). Heidelberg: Springer.
- Balli, F., Balli, H. O., & Louis, R. J. (2016). The impacts of immigrants and institutions on bilateral tourism flows. *Tourism Management* 52 , 221-229.
- Beck, T., & Levine, R. (2005). Legal Institutions and Financial Development . In C. M. (eds.), *Handbook of New Institutional Economics* (pp. 251-278). Dordrecht: Springer.
- Chaisumpunsakul, W., & Pholphirul, P. (2018). Does international trade promote international tourism demand? Evidence from Thailand's trading partners. *Kasetsart Journal of Social Sciences* 39 , 393-400.
- COMCEC. (2019). *COMCEC Tourism Outlook 2019*. Ankara: COMCEC Coordination Office.
- Detotto, C., Giannonia, S., & Goaveca, C. (2021). Does good governance attract tourists? *Tourism Management* 82 , 104-155.
- Hall, P., & Taylor, R. (1996). Political Science and the Three New Institutionalism. *Political Studies*, 44, 936-957.
- Honey, M., & Gilpin, R. (2009). *Tourism in the Developing World: Promoting Peace and Reducing Poverty* . Washington: US Institute of Peace .
- Jiang, T., Zhuo, S., Zhang, C., & Gao, J. (2019). The Impact of Institutions on the Evolution of Tourism Accommodation Format: Evidence from Wulingyuan, China. *Sustainability, MDPI, Open Access Journal*, vol. 11(10),, 1-1.
- Kaufmann, D., Kraay, A., & Mastruzzi, M. (2010). *The Worldwide Governance Indicators Methodology and Analytical Issues* . The World Bank.
- Klein, P. A. (1993). The institutionalist Challenge: Beyond Dissent. In M. R. Tool, *Institutional Economics: Theory, Method, Policy* (pp. 245-270). Massachusetts: Kluwer Academic Publishers.
- Moshirian, F. (2008). Globalisation, growth and institutions . *Journal of Banking & Finance* 32 , 472-479.
- Mushtaq, R., Thoker, A. A., & Bhat, A. A. (2020). Does institutional quality affect tourism demand? Evidence from India. *Journal of Hospitality and Tourism Insights Vol. ahead-of-print No. ahead-of-print*.
- North, D. C. (1990). *Institutions, Institutional Change and Economic Performance*. Cambridge: CAMBRIDGE UNIVERSITY PRESS.
- Peters, B. (1999). *Institutional Theory in Political Science the ' New Institutionalism'*. New York: PINTER.
- Roxas, B., & Chadee, D. (2013). Effects of formal institutions on the performance of the tourism sector in the Philippines: The mediating role of entrepreneurial orientation . *Tourism Management* 37 , 1-12.
- Sabir, S., Rafique, A., & Abbas, K. (2019). Institutions and FDI: evidence from developed and developing countries. *Financial Innovation* 5:8, 1-20.
- Shepsle, K. A. (2006). RATIONAL CHOICE INSTITUTIONALISM. In R. A. RHODES, S. A. BINDER, & B. A. ROCKMAN, *The Oxford Handbook of Political Institutions* (pp. 23-39). New York: Oxford University Press.

Yap, G. C., & Saha, S. (2013). Do political instability, terrorism, and corruption have deterring effects on tourism development even in the presence of unesco heritage? A cross-country panel estimate. *Tourism Analysis*, 18, 587-599.

APPENDIX

TABLE 4: LIST OF COUNTRIES

Albania	Georgia	Lebanon	Peru
Angola	Ghana	Madagascar	Philippines
Argentina	Guatemala	Malawi	Qatar
Armenia	Guinea-Bissau	Malaysia	Romania
Azerbaijan	Haiti	Mauritius	Russian Federation
Bahrain	Ecuador	Moldova	Saudi Arabia
Belarus	Egypt, Arab Rep.	Mongolia	Serbia
Bolivia	El Salvador	Morocco	Sierra Leone
Bosnia and Herzegovina	Ethiopia	Mozambique	South Africa
Botswana	Gambia, The	Myanmar	Sri Lanka
Brazil	Honduras	Mexico	Sudan
Bulgaria	Hungary	Namibia	Thailand
Cambodia	India	Nepal	Timor-Leste
Cameroon	Indonesia	Nicaragua	Tunisia
Chile	Iraq	Nigeria	Turkey
China	Jamaica	North Macedonia	Uganda
Colombia	Jordan	Oman	Ukraine
Costa Rica	Kazakhstan	Pakistan	Uruguay
Croatia	Kuwait	Panama	Uzbekistan
Dominican Republic	Kyrgyz Republic	Paraguay	Vietnam
			Zambia