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Economic Accountability in the Context of Local Governance in the Philippines: A Structural Equation Modelling Approach

Hernan Banjo G Roxas, Val Lindsay, Nicholas Ashill and Antong Victorio

This study posits that by virtue of the enabling role of local governments, the economic development of their locality must be at the core of their public accountability, which is referred to here as “economic accountability”. Grounded on this idea of accountability, along with enabling theory and institutional theory, the study presents empirical evidence supportive of the argument that the enabling role of local governments, as manifested in a capacity to establish or adhere to formal institutional arrangements, has a direct impact on the entrepreneurial strategic posture and performance of local small and medium enterprises (SMEs) which are key players in local economic development. The results of the structural equation modelling support the view that institutional arrangements as manifestations of the enabling role of city governments are positively associated with an entrepreneurial strategic posture of local firms, which consequently improves the firms’ overall economic performance. Therefore, SME development in particular, and local economic development in general, should be part of the economic accountability of local governments in the Philippine context of local governance.

Introduction

The decentralisation of governance bestowed on local governments new roles, powers and responsibilities, including the role of enabling or nurturing local economic growth and development (Brillantes 2004; Legaspi 2001). This is particularly true in the Philippines whereby decentralisation in its various forms has been an integral part of government reforms since the enactment of the 1991 Local Government Code. However, the paucity of empirical evidence on the direct link between local government actions and local economic development prohibits the process of making local governments directly accountable for local economic development. This lack of “economic accountability” severely limits the concept of public accountability ascribed to local governments. In effect, the exercise of public accountability at the local government level remains elusive to the overall goal of serving the public interest of the local citizenry.

Public accountability, involving the obligation to present an account of and answer for the execution of responsibilities to those who entrusted those responsibilities (Gray & Jenkins 1986; Kluvers 2003), is an important
element of good governance. The current research issue is on knowing who is accountable to whom and for what (Eckardt 2008). This view on public accountability entails not just providing information or answering questions but extends to activities such as setting goals and providing and reporting on results, and to the visible consequences of getting things right or wrong (Parker & Gould 1999). The emphasis on consequences, results, outcomes or impacts implies that performance evaluation is crucial in attributing which roles and responsibilities local governments must be held accountable for. Local governments can only be held publicly accountable for actions (as policies, programmes and projects) for which there is empirical evidence that such actions have produced appropriate, desirable or undesirable outcomes (Cameron 2004; Eckardt 2008; Kluvers 2003).

The use of citizen feedback such as report cards from surveys is a popular form of evaluating local government performance, as well as improving transparency and public accountability (Thampi & Sekhar 2006). In the Philippines, for instance, the biennial survey as part of the Philippine Cities Competitiveness Ranking Project (PCCRP) (Magdaluyo, et al 2001) provides a scorecard on the business climate of Philippine cities, which includes an evaluation of the efficiency and effectiveness of the city government from the point of view of small and medium enterprises (SMEs).

What is missing in projects like the PCCRP is the empirical evidence that the evaluation scores really matter because they have direct and measurable impact on SMEs or on whoever is making such an evaluation. Only then can public accountability be made meaningful and practical which deserves government action or rectification. The citizen feedback mechanism becomes useful if it does not only evaluate government actions, but also spells out the felt or perceived effects of those actions.

Given these information gaps, this study provides empirical evidence on the economic accountability of local governments by identifying a set of formal institutional arrangements established or adhered to by two city governments in their respective cities and measuring how these arrangements relate to the entrepreneurial strategic posture and performance of local SMEs. The focus is on SMEs being the key players in local economic development in many developing countries like the Philippines (APEC 2003; OECD 2003, 2005). Through a survey, the study asks SMEs to evaluate the arrangements, thereby generating a “citizen report card”. SMEs were also asked to evaluate their entrepreneurial strategic posture or the extent to which they engage in risk-taking, proactive and innovative activities within their businesses (Covin & Slevin 1989), as well as their overall organisational performance.

Using a structural equation modelling technique, the study seeks to establish the direct relationships between local government institutional arrangements and the entrepreneurial strategic posture and performance as perceived and reported by the SMEs. The aim is to substantiate the view
that local governments have, and should be concerned with, economic accountability. The rationale is that the quality of the institutional arrangements they put in place or adhere to has a significant impact on the entrepreneurial activities of local firms within their jurisdictions, which ultimately shapes the trajectory of local economic development.

**Enabling Role of Local Governments in Local Economic Development**

In a decentralised system of governance as in the Philippines, local governments exercise substantial fiscal and political autonomy, as well as various roles and functions designed to increase accountability and responsiveness of government services to local preferences (Brillantes 2004; Eckardt 2008). Local governments are expected to assume a leading role in the local economy by developing various forms of intervention to bring about more economic development activities in the community (Legaspi 2001). This particular role is at the core of the enabling model of local governance, which holds that local governments should provide the mechanisms and incentives to pave the way for more economic activities in the community (Leach, Stewart & Walsh 1994). Local governments can organise interventions in the local economy as a means of stimulating economic activities, and can provide the necessary framework for more private sector participation in local developmental activities (Legaspi 2001).

The fundamental tenet of the model views economic, social and political gains as best achieved by local governments developing their roles far beyond that of directly administering a limited range of services (Smith 2000).

Local governments can perform their enabling role by exercising market-enabling authority, which is subsumed under Smith’s (2000) concepts of community planning and community leadership. The exercise of market-enabling authority demands that local governments take a leading role in planning and coordinating local economic development through partnerships, facilitation, cooperation, advocacy, consultation, and grants-in-aid (Smith 2000). It entails the freeing of local factor markets and the removal of the obstruction of bureaucratic, tax and associated anti-business requirements (Imrie & Raco 1999). Local governments play an active role in ensuring that the goals of local economic development form an important part of the overall development agenda.

Local economic development has become a primary preoccupation of many local governments in the Philippines (Brillantes 1999; Legaspi 2000, 2001). It has become the major focus of governance as local governments seek to generate jobs, boost incomes, and raise tax revenues (Imrie & Raco 1999). Local economic development can be viewed as a process of stimulating or maintaining business activities and employment by maximising the utilisation of the intellectual, social, physical and cultural capital of the local community (Blakely & Bradshaw 2002).
The role of small and medium enterprises (SMEs) in local economic development cannot be overemphasized. Comprising over 98 percent of total enterprises in the Asia-Pacific region (APEC 2002), SMEs have assumed a leading role in the economic development of many countries (Benney 2000; Lee & Peterson 2000; OECD 2005). In the Philippines, 99.6 percent of the total 810,362 business establishments as of 2003 were small (including micro) and medium firms generating 67.9 percent of the country’s total employment (DTI 2005). The impact of the SME sector on the overall economic development of the country, regions and cities is no longer debatable (Acs, Arenius, Hay & Minniti 2004; Allen, Langowitz & Minniti 2007; APEC 2003). Yet the liability of smallness explains that, despite their potential to contribute to economic growth, SMEs are unable to compete well because of various constraints, including unsupportive institutional environmental issues (Kirby & Watson 2003; Lall 2000).

Critical to the success of SMEs is their capacity to exercise an entrepreneurial strategic posture (involving the top management’s risk taking behaviour with regard to investment decisions and strategic actions in the face of uncertainty), the extensiveness and frequency of product innovations and the related tendency toward technological leadership, and the pioneering nature of the firms as evident in their propensity to compete with industry rivals aggressively and proactively (Covin & Slevin 1990; Covin, Slevin & Schultz 1994; Gibbons & O’Connor 2005).

Strategic posture implies that a firm can be categorised along a continuum ranging from less entrepreneurial to more entrepreneurial (Covin 1991; Covin & Slevin 1990). Strategic posture, while exercised by the owner of a SME or top management of a firm, is considered to be an organisational variable, as organisations are reflections of the values and cognitive bases of powerful actors (Carpenter & Fredrickson 2001). Such a posture hinges on three fundamental constructs: innovativeness, proactiveness, and risk-taking. Innovativeness reflects a tendency to support new ideas, novelty, experimentation, and creative processes, thereby departing from established practices and technologies (Lumpkin & Dess 1996). Proactiveness refers to a posture of anticipating and acting on future wants and needs in the marketplace, thereby creating a first-mover advantage vis-à-vis competitors (Lumpkin & Dess 1996). Risk-taking is associated with a willingness to commit large amounts of resources to projects where the cost of failure may be high (Miller & Friesen 1982). Strategic posture thrives in an institutional environment that is supportive of risk-taking, innovativeness and proactiveness.

Public Accountability

Public accountability is an important element of good governance. It involves being answerable for decisions or action, often to prevent the misuse of power and other forms of inappropriate behaviour (Cameron
It is an obligation to present an account of and answer for the execution of responsibilities to those who entrusted those responsibilities (Gray & Jenkins 1986; Kluvers 2003; Parker & Gould 1999).

Although public accountability is difficult to define (Cavill & Sohail 2004; Parker & Gould 1999), what is clear in the literature is that the concept of accountability does not simply imply providing information or answering questions, but extends to the setting of goals, the reporting of results, and the acceptance of responsibility for the consequences of getting things right or wrong (Parker & Gould 1999). Hence it involves the giving of an account, and being held to account (Wilson 1998), along with an evaluation of the performance of the entity that is accountable for a specific action (Parker & Gould 1999). The challenge is to determine who is accountable to whom and for what (Eckardt 2008).

As a form of enforcing public accountability, citizen report cards or scorecards are regarded as a convenient and effective means of evaluating local government performance (Deichmann & Lall 2003). They articulate citizens’ assessment of public services, provide evidence of inefficiency and corruption, and stimulate public service providers to be more responsive to their clients (Paul 1998). They are a simple and widely replicable tool for improving transparency and public accountability. They provide benchmarks on the accessibility, adequacy and quality of public services as experienced by citizens, along with measures of citizen satisfaction to prioritise corrective actions, indicators of problem areas in the delivery of public services, and mechanisms for exploring citizens’ alternatives for improving public services (Thampi & Sekhar 2006).

Notwithstanding their value, little is known about the impact of citizen report cards on citizens in general, on those who are doing the evaluations, and on those sectors which are the beneficiaries of particular government policies or programmes. Scorecards on the competitiveness of cities used by the Asian Institute of Management in the Philippines (Magdaluyo, et al 2001) do not include measures on whether a competitive city also equates to its having competitive business enterprises. A report card that measures only one side of the equation is of limited value for the purposes of governmental improvement.

The Research Model and Hypotheses

The public accountability model provides the theoretical base of this study, with the triangular relationships between a local government in general, the more specific service provider(s), and the citizens constituting the accountability relationships (Paul 1992; World Bank 2003). With regard to service delivery, the model distinguishes between the “long route of accountability” or “voice” that implies accountability of the elected government officials and their ability to channel community demands through to the service providers, and the “short route of accountability”
or “client power” which implies direct accountability of service providers to the general public (Cavill & Sohail 2004; Eckardt 2008; Paul 1992). The focus here is on both routes of accountability, such that a local government can be held accountable to its constituent SMEs, and the different offices within it can be held directly accountable to SMEs concerning the provision of government services (including business permits and licensing) and the extent of smooth government-to-business transactions.

The study builds on North’s (1990) institutional theory in the identification of the different institutional arrangements which a local government can set up or adhere to within its jurisdiction to manage its affairs. North (1990) defines institutions as the legal and political structures and processes in a city that explicitly specify and enforce the rights, duties, responsibilities and privileges of its local populace (including business entities) and govern the interrelationships among them (Fogel, Hawk, Morck & Yeung 2006). These institutional arrangements are the rules of the game which specify the incentives and constraints on economic activity within the city (North 1990). As shown in Figure 1, they are presented as having a direct impact on the entrepreneurial strategic posture of SMEs, which in turn has a direct impact on the overall performance of local firms.

![Figure 1 The Conceptual Model](image)

Several theories and empirical studies have noted the importance of the rule of law, protection of property rights, and so on for business performance, entrepreneurship and economic development (Aidis 2005; Manolova, Eunni & Gyoshev 2008; Roxas, Lindsay, Ashill & Victorio 2007; Welter & Smallbone 2005). Based on this material and the above discussion, the study advances the following hypotheses:

H₁ – The rule of law is positively associated with entrepreneurial strategic posture.
H₂ – The protection of property rights is positively associated with entrepreneurial strategic posture.
H₃ – Government policies perceived as conducive to SME business activity are positively associated with an entrepreneurial strategic posture.
H₄ – Regulatory quality is positively associated with an entrepreneurial strategic posture.
H₅ – Government assistance is positively associated with an entrepreneurial strategic posture.

Strategies are the mechanisms by which firms manage their relationships with the external environment and serve as the basic driving force in their value-creating processes in all functional areas of their businesses (Swamidaas & Newell 1987). This creation of value is manifested in a firm’s organisational performance. Several studies have cited the positive effects of an entrepreneurial strategic posture on various facets of organisational performance (Covin & Miles 1999; Wiklund 1999; Wiklund & Sheperd 2005). Hence, it is further hypothesised that:

H₆ – An entrepreneurial strategic posture is positively associated with organisational performance.

Research Method

Sample and Study Setting

The survey retrieved 955 (68.21%) of the 1,400 distributed questionnaires distributed in two cities in the south-eastern region of the Philippines. The relatively high response rate could be attributed to the use of enumerators who distributed and retrieved the questionnaires as opposed to using the postal service.

To account for possible variations in formal institutional arrangements due to the resources held by city governments, the two cities were chosen on the basis of their income classification. Hence one city was chosen as being a first class (high income) city, while the other was identified as a fourth class (low income) city. Although the unit of analysis was at the firm or enterprise level, the actual survey respondents were owners/managers of SMEs duly registered with their respective city governments.

Of the total retrieved questionnaires, 900 were usable. They related to 271 manufacturing firms (267 small and 4 medium enterprises) and 629 service firms (excluding trading firms) (627 small and 2 medium sized firms).

In terms of city location, 454 firms (161 manufacturing firms and 293 service firms) were from City A, and 446 (110 manufacturing firms and 336 service firms) were from City B. While the average age of the sample firms was 6.33 years, the youngest was 1 month and the oldest 40 years. Some
85 percent were less than 10 years old. Of the total respondent firms, 107 reported only one employee, 224 reported two employees, and 160 reported three employees. Firms with less than four employees accounted for 55 percent of the total sample.

Wave analysis did not reveal any non-response bias (Lankford, Buxton, Hetzler & Little 1995; Rogelberg & Stanton 2007). Results of Harman’s single factor test and a partial correlation analysis using a marker variable suggested that mono-method bias was not a concern (Hair, Black, Babin, Anderson & Tatham 2006). Using SPPS v14, a missing values analysis was performed and subsequently a mean substitution was applied because of the missing (completely at random) nature of the values. The distribution of data was considered within the normal range with respect to skewness and kurtosis indices.

**Measurement**

Indicators to measure the significance of institutional arrangements were adopted from previous studies on institutional and governance quality (Frye & Zhuravskaya 2000; IMD 2006; La Porta Lopez-de-Silanes, Shleifer & Vishny 1999; World Bank 2002), business climate and national competitiveness (IFC 2007; Lopez-Claros, Altinger, Blanke, Drzeniek & Mia 2007), and institutional environments (Busenitz, et al 2000; Fogel, et al 2006). The items elicited the extent of agreement or disagreement (in a seven-point Likert scale) of the respondents on the institutional arrangements presented in Figure 1. The perceptual measurement of these arrangements is consistent with the concept of “perceived and enacted environment”, which suggests that it is the firm owners'/managers' perception of the institutional environment that matters in organisational strategic processes (Bourgeois 1980; Oswald, Mossholder & Harris 1997; Weick 1988). This method of evaluating institutional arrangements is very similar to the typical citizen report card used in other studies (eg, Magdaluyo, et al 2001).

Entrepreneurial strategic posture comprises nine items adopted from Covin and Slevin's (1989) work in which responses to statements are expressed in a seven-point scale, with 7 reflecting an entrepreneurial strategic posture and 1 reflecting a less entrepreneurial strategic posture. Organisational performance is measured by four items dealing with sales, net income, market share and return on investment (ROI). These four indicators have been shown in previous studies to be adequate performance measures (Baker & Sinkula 2005; Rowe & Morrow 1999; Venkatraman & Ramanujam 1986; Westhead & Howorth 2006).

Respondents were asked to rate the level of importance they attached to each of the performance indicators. They were subsequently asked to express their perception on their level of performance on these indicators relative to their competitors in the last three years. The importance scores were multiplied by the perceived performance scores to generate the
weighted performance scores for each of the four performance indicators. This approach is consistent with previous studies that have addressed firm performance (Delaney & Huselid 1996; Naman & Slevin 1993). Perceptual measures of performance have been shown to be valid and reliable and, therefore, have an acceptable level of utility for empirical research (Dess & Robinson 1984).

Data Analysis

Structural equation modelling (SEM) was used to test the hypotheses of the study, aided by the software called EQS 6.1 (Bentler 1995). SEM is a multivariate statistical technique to confirm the causal relationships of latent variables in a model strongly guided by theory. Using Anderson and Gerbing’s (1988) two-step approach, the study developed and confirmed an effective measurement model using confirmatory factor analysis, with the structural model depicting the hypothesised relationships of the constructs.

Confirmatory factor analyses (CFA) were performed on the institutional features, entrepreneurial strategic posture, and organisational performance using the maximum likelihood technique (Brown 2006). CFA is a tool that seeks to determine if the number of factors and the loadings of measured indicators or variables on the factors conform to what is expected on the basis of pre-established theory (Mueller 1996; Thomson 2004). The indicators or items were pre-selected or assumed to load to a specific factor or construct based on prior strong theoretical, conceptual or empirical evidence (Brown 2006; Hair, et al 2006). Details of the CFA are shown in Table 1.

Initial results of the CFA on institutional arrangements required a re-specification of the measurement model, aided by the modification index called Lagrange Multiplier (LM) and the Wald tests provided by EQS (Bentler 1995). Results of the LM and Wald tests indicated that a significant improvement in the goodness-of-fit measures could be gained (as shown in model B in Table 2) by dropping two items (with factor loadings below .5) that measured the protection of property rights and by combining the remaining items with that of the rule of law. All of the combined items are subsumed under the rule of law. Previous studies have shown the very close and substantive theoretical linkage between the rule of law and the protection of property rights (Frye & Zhuravskaya 2000; Reed 2001). Model modification is warranted if there is a substantial theoretical basis for it (Byrne 2006).

The CFA results show that all of the items measuring entrepreneurial strategic posture and organisational performance loaded highly on the pre-determined factors, with no path estimate lesser than the .5 minimum value (Brown 2006). All constructs show an acceptable level of reliability as evidenced by the highest internal consistency coefficients (ie, Cronbach α).
Table 1  
Confirmatory Factor Analysis

<table>
<thead>
<tr>
<th>FACTORS and ITEMS</th>
<th>Standardised Factor Loading*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rule of Law (AVE = .79)</td>
<td>α = .91</td>
</tr>
<tr>
<td>occurrence of crime does not impose business costs</td>
<td>.92</td>
</tr>
<tr>
<td>efficient legal framework to challenge government actions</td>
<td>.86</td>
</tr>
<tr>
<td>fair and impartial judicial system</td>
<td>.89</td>
</tr>
<tr>
<td>effectiveness in enforcing commercial contracts.</td>
<td>.88</td>
</tr>
<tr>
<td>legal means rather than force to settle disputes</td>
<td>.89</td>
</tr>
<tr>
<td>people comply with court rulings</td>
<td>.91</td>
</tr>
<tr>
<td>prosecution of violations of property rights</td>
<td>.87</td>
</tr>
<tr>
<td>protection of intellectual property rights</td>
<td>.91</td>
</tr>
<tr>
<td>Government Policies (AVE = .84)</td>
<td>α = .96</td>
</tr>
<tr>
<td>taxation laws and policies</td>
<td>.86</td>
</tr>
<tr>
<td>effective implementation of government decisions</td>
<td>.97</td>
</tr>
<tr>
<td>economic policies adapt to changes in the economy.</td>
<td>.92</td>
</tr>
<tr>
<td>clear and consistent policy direction</td>
<td>.97</td>
</tr>
<tr>
<td>Laws and regulations conducive for business.</td>
<td>.86</td>
</tr>
<tr>
<td>Regulatory Quality (AVE = .81)</td>
<td>α = .97</td>
</tr>
<tr>
<td>information about laws and regulations</td>
<td>.96</td>
</tr>
<tr>
<td>business regulations</td>
<td>.86</td>
</tr>
<tr>
<td>procedures in city government transactions</td>
<td>.95</td>
</tr>
<tr>
<td>number of government offices to deal with</td>
<td>.93</td>
</tr>
<tr>
<td>number of permits required</td>
<td>.88</td>
</tr>
<tr>
<td>time required to register a business</td>
<td>.90</td>
</tr>
<tr>
<td>interpretations of the laws and regulations</td>
<td>.91</td>
</tr>
<tr>
<td>number of city government inspections required</td>
<td>.81</td>
</tr>
<tr>
<td>Government Assistance (AVE = .59)</td>
<td>α = .88</td>
</tr>
<tr>
<td>sponsorship of new businesses</td>
<td>.76</td>
</tr>
<tr>
<td>special support to start a new business.</td>
<td>.71</td>
</tr>
<tr>
<td>assistance to start own business.</td>
<td>.80</td>
</tr>
<tr>
<td>after failing in an earlier business, assistance in starting again.</td>
<td>.84</td>
</tr>
<tr>
<td>government contracts for new and small businesses.</td>
<td>.74</td>
</tr>
</tbody>
</table>
Economic Accountability in the Context of Local Governance in the Philippines

Entrepreneurial Strategic Posture (AVE = .75)  \( \alpha = .94 \)
- tried and tested products/services vs. R & D, technological leadership  .83
- no. of new product/service lines in past few years  .89
- minor vs. dramatic changes in product/service lines  .87
- proactive vs. responsive dealings with competitors  .87
- introduction of new products/techniques/technologies  .86
- avoid vs. adopt competitive posture  .83
- preference for low risk vs. high risk projects  .89
- cautious vs. bold acts to explore business environment  .85
- cautious vs. bold decision-making  .91

Organisational Performance (AVE = .61)  \( \alpha = .76 \)
- sales  .80
- market share  .68
- net income  .86
- return on investment  .78

\*all significant at .05 (i.e. test statistic > ± 1.96)

AVE = average variance extracted based on standardised solution
\( \alpha = \) Cronbach alpha

Table 2
Goodness-of-Fit Measures

<table>
<thead>
<tr>
<th>Constructs</th>
<th>( \chi^2 )</th>
<th>NFI</th>
<th>CFI</th>
<th>RMSEA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Formal Institutions - Model A</td>
<td>10,350.49, 350 df, ( p = .00 )</td>
<td>.68</td>
<td>.69</td>
<td>.18</td>
</tr>
<tr>
<td>Formal Institutions - Model B</td>
<td>8,574.95, 299 df, ( p = .00 )</td>
<td>.92</td>
<td>.91</td>
<td>.06</td>
</tr>
<tr>
<td>Informal Institutions</td>
<td>427.85, 356 df, ( p = .01 )</td>
<td>.92</td>
<td>.98</td>
<td>.02</td>
</tr>
<tr>
<td>Strategic Posture</td>
<td>612.93, 27 df, ( p = .00 )</td>
<td>.93</td>
<td>.93</td>
<td>.14</td>
</tr>
<tr>
<td>Organisational Performance</td>
<td>4.37, 2 df, ( p = .11 )</td>
<td>.99</td>
<td>.99</td>
<td>.03</td>
</tr>
</tbody>
</table>

Model A - retained all factors and items
Model B - retained all factors/items but combined all items for rule of law and protection of property rights and dropped two items under protection of property rights

NFI - Bentler-Bonnett’s Normed Fit Index
CFI - Comparative Fit Index
RMSEA - Root Mean-Square Error of Approximation

27
Convergent validity is indicated by the fact that the items loaded significantly (ie, $t > 1.96$) on their corresponding construct with the lowest $t$-value being 12.05 (Bagozzi, Yi & Phillips 1991). In determining the discriminant validity of the constructs, the correlations among the latent constructs were examined to check if the values were significantly less than one. Results indicate that none of the confidence intervals of the $\phi$ values (+ two standard errors) include the value of one, thereby providing the evidence of discriminant validity (Bagozzi & Yi 1988). Further evidence of convergent validity were the average variance extracted (AVE) values which were all above the threshold of .50, indicating that the constructs contained less than 50 percent error variance (Fornell & Larcker 1981). Discriminant validity was further established after knowing that the square root of each construct’s AVE was found to be larger than its correlations with other constructs, as shown in Table 2 (Fornell & Larcker 1981; Hair, et al 2006).

The overall goodness-of-fit indices indicate that the measurement model fits the data well, as evidenced by the goodness-of-fit measures. The results of the ROBUST Method offered by EQS to examine the model in case of slight departures from the normality assumption of data distribution confirm the results generated by the maximum likelihood technique.

Overall, the results of the test of the measurement model-data fit suggest that the constructs used in this study possess a satisfactory level of construct validity, internal consistency (ie, reliability), and convergent as well as discriminant validity. Table 3 shows the means, standard deviation and correlations of the six constructs used in the succeeding analysis of the structural model-data fit.

Hypothesis Testing

Results from fitting the structural model to the data using the maximum likelihood technique show satisfactory results, as shown by the goodness-of-fit measures in Figure 2. Because Mardia’s coefficient of 30.51 was far above the maximum threshold of 5.00 (Byrne 2006) indicative of non-

<table>
<thead>
<tr>
<th>Variables</th>
<th>Mean</th>
<th>SD</th>
<th>RL</th>
<th>GP</th>
<th>RQ</th>
<th>GA</th>
<th>SP</th>
<th>OP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rule of Law (RL)</td>
<td>4.62</td>
<td>1.30</td>
<td>.89</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Government Policies (GP)</td>
<td>4.30</td>
<td>1.77</td>
<td>.88*</td>
<td>.92</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Regulatory Quality (RQ)</td>
<td>4.30</td>
<td>1.53</td>
<td>.87*</td>
<td>.80*</td>
<td>.90</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Government Assistance (GA)</td>
<td>2.28</td>
<td>.88</td>
<td>.25*</td>
<td>.24*</td>
<td>.21*</td>
<td>.77</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Entrepreneurial Strategic Posture (SP)</td>
<td>3.62</td>
<td>1.38</td>
<td>.86*</td>
<td>.81*</td>
<td>.79*</td>
<td>.35*</td>
<td>.87</td>
<td></td>
</tr>
</tbody>
</table>
| Organisational Performance (OP) | 14.88 | 3.75 | .47*| .45*| .42*| .13*| .49*| .78 *

*Significant at the .01 level (2-tailed)
**Significant at the .05 level (2-tailed)

square root of average variance extracted (ave) values in diagonal and bold figures
normal distributions, the ROBUST technique was also applied using EQS. The output confirms the maximum likelihood technique results. Further details are shown in Figure 2.

The results show that all of the variables have variances that are statistically different from zero, which indicate that each variable is highly distinguishable (i.e., distinctive) from one another (Bentler 1995). All of the institutional arrangements explain 65 percent of the variations in the firms’ entrepreneurial strategic posture, while the latter explains 29 percent of the variations in the firms’ organisational performance. The rule of law has the largest impact on entrepreneurial strategic posture, followed by government policies and regulatory quality. The empirical evidence indicates that all of the arrangements are positively associated with an entrepreneurial strategic posture, supporting $H_1$, $H_3$, $H_4$, and $H_5$. $H_2$ was not tested due to the psychometric issues associated with the protection of property rights. Strategic posture, on the other hand, showed a positive significant relationship with organisational performance – a result that is consistent with $H_6$. 

**Figure 2**

The Structural Model

- Government Assistance ($\gamma = 0.68^{**}$)
- Regulatory Quality ($\gamma = 4.25^{**}$)
- Government Policies ($\gamma = 1.78^{**}$)
- Rule of Law ($\gamma = 2.89^{**}$)
- Entrepreneurial Strategic Posture ($\gamma = 0.88^{**}$)
- Organisational Performance ($\gamma = 7.12^{**}$)

**Goodness of Fit Measures:**

$\chi^2 = 12,092.81, \text{df} (p > .000), \text{NFI} = .92, \text{CFI} = .94, \text{RMSEA} = .06$

$\gamma =$ variance, **significant at $p < .05$, (standard errors)

control: city location
The \( r^2 \) values (being the derivatives of the Pearson \( r \)), suggest that the effect sizes for the institutional features \( \rightarrow \) strategic posture paths and strategic posture \( \rightarrow \) organisational performance path are considered medium and large effects, respectively (Field 2005). These indicators of effect size suggest that, despite having relatively small yet significant path coefficients, the results could be considered practically significant and meaningful, from which inferences could be drawn (Cohen 1992; Field 2005; Pedhazur 1982).

Conclusions

The empirical evidence shows that all of the institutional arrangements established or adhered to by the two local governments in managing the socio-political and economic affairs of their respective cities are positively associated with local firms’ entrepreneurial strategic posture. Results indicate that SMEs are likely to report higher levels of entrepreneurial strategic posture when they perceive that the rule of law prevails in the city, that government policies are conducive to business, that regulatory quality does not impose an unnecessary burden on business enterprises, and that there is government assistance which business enterprises can draw on. Likewise, when SMEs report higher levels of entrepreneurial strategic posture, they are also likely to report higher levels of perceived organisational performance.

The results further suggest that when a local government is able to ensure such an institutional environment, local firms like SMEs are likely to become proactive in taking risks to explore more business opportunities. SMEs are also likely to invest in innovation which can generate more products and services and better ways of production. These activities will open up employment opportunities as the home-grown business sector grows, thereby propelling local economic development.

In effect, the empirical evidence supports the view that a scorecard measuring institutional arrangements of significance to local governments is a valid evaluation mechanism with respect to the performance of the enabling role of local governments. The performance of local governments in terms of the arrangements is evidence of the crucial role local governments play in local economic development. To pursue local economic development through the development of SMEs, local governments need to review the efficiency and effectiveness of the arrangements as part of the overall governance of the locality or city.

The impact of the scorecard’s results on the entrepreneurial strategic posture of SMEs lends support to the view that local governments’ overall public accountability must include economic accountability. By enforcing economic accountability, local governments are encouraged to become conscious of their enabling authority in local economic development, knowing that their enabling role will have a substantial and measurable
impact on the local community and its various sectors such as SMEs. Finally, the study highlights the need to develop citizen report cards or scorecards that measure the actions of local governments, as well as the outcomes and impacts of those actions. Only then can economic accountability become truly meaningful, constructive and useful.

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Economic Accountability in the Context of Local Governance in the Philippines


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Economic Accountability in the Context of Local Governance in the Philippines


Banjo Roxas is Junior Research Officer in the New Zealand Centre for SME Research at Massey University, Val Lindsay is Head of the School of Marketing and International Business at Victoria University of Wellington (VUW), Nicholas Ashill is Associate Professor in the School of Marketing and International Business, VUW, and Antong Victorio is Senior Lecturer in the School of Government, VUW.

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