Corruption Is also a Challenge to Rich Countries

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International publication, October 2004

Conventional wisdom has long associated corruption with the public sector in poor countries, with rich ones held up as models of integrity and good governance. However, corruption itself has been narrowly defined as illegal activity—most notably bribery —ignoring less conspicuous "legal" forms of corruption, such as influence-peddling, pressure by vested interests, and outright capture by elite corporations. This narrow view has resulted in worldwide corruption indicators that have perpetuated the perception that poor countries and corrupt, while the rich world is clean.

Long overdue is a broader interpretation of corruption, which accounts for the undue benefits actively pursued by the private, powerful few as they shape state institutions, policies, laws and regulations to their own ends. The measurement and analysis of corruption within this broader definition is now possible, thanks to new data analysis contained in the World Economic Forum's forthcoming Global Competitiveness Report. This new comprehensive dataset was obtained through the Forum's Executive Opinion Survey, containing answers from over 8,700 business leaders in 104 countries to a wide range of questions concerning business environment conditions. In sharp contrast with the conventional approach to past measures of corruption, the data indicates that there is wide variation in ethical standards across all countries, rich and poor.

In an effort to tease out the complex interrelationship between governance, corruption, and competitiveness in business, a unique set of ethics indices was designed to get at the de facto obstacles affecting businesses, and to probe more deeply into such issues as legal corruption, undue influence and corporate ethics, extent of bribery by firms operating abroad, and the firm's perceptions of the cost of terrorism, crime and money laundering. To say the least, the results are sobering.

The Survey asks firms to evaluate a list of 14 problematic factors for doing business in their country and to select and rank the top five. As one might expect, emerging countries listed corruption, policy instability and financing as among the most problematic, while the wealthy countries (largely OECD members) saw labor regulations, bureaucracy, and taxes as the leading obstacles. Overall, the governance cluster, comprising corruption and excessive bureaucracy, surfaced as a key constraint in 79 out of the 104 countries surveyed, including in many OECD members.

First, the evidence sheds light on the complex challenges across different regulatory regimes. In some key dimensions, the evidence reveals a striking gap not so much between OECD and emerging economies, but between particular sub-regions. It is telling, for instance, that the newly-industrializing countries (NICs) of East Asia report fewer obstacles to business entry than the average for those in OECD members, reflecting the highly regulated nature of many economies in the latter. The gap between the exemplary East Asian NICs, on the one hand, and the laggards in Latin America and in the former Soviet Union, on the other, is particularly acute. There are similarly striking gaps among different subgroups within the OECD. The Nordic countries report exemplary ease of entry to firms, in sharp contrast to southern Europe, which also report greater restrictions on business startups than in Eastern Europe.

The window provided by the Survey on what is actually taking place on the ground challenges the undue focus on official statistics or de jure counting of number of steps or codification of the technical requirements for starting a business. In short, while the laws and rules in the books do matter, it is how these rules are implemented that have a most direct bearing on business functioning, and hence on a country's competitive edge.

In order to see how competitiveness is affected by these factors, the study probed statistically the link between the various constraints to business given by the firms, and their rankings in the Growth Competitiveness Index (GCI) developed by the World Economic Forum. We found that among the list of 14 obstacles to business, corruption had the highest impact on the GCI. The payoff from addressing corrupttion is indeed the largest: a country undergoing a serious but realistic improvement in controlling corruption could on average enhance its worldwide competitiveness ranking by about 30 positions; clearly a very substantial payoff.

Can this be simply the outcome of the rich-poor country global divide? To answer this question, ethics indices were developed to measure corporate legal, illegal, public sector, judicial and governance behaviors. No one disputes that outright domestic bribery is illegal and relatively infrequent within OECD countries, though it amounts to large sums, due to the sheer economic size of these states. However, despite the adoption of the OECD cross-border Anti-Bribery Convention, the study shows that firms based in OECD countries operating abroad do in fact "adapt" to the realities of their host countries, and tend to engage in outright bribery with far greater frequency than in their home base.

Arguably the more surprising findings in this study concern the extent of 'privatization' of public policy, which encompasses manifestations of legal corruption such as the creative use of loopholes for political financing that skews law-making and policies, favoritism in procurement, and so on, all within the law in the strict sense, yet far from being ethically untainted. With corruption thus more broadly defined, it was found that the so-called rich countries do not perform in an uniformly stellar fashion. While the Nordic countries do well on these measures of legal corruption, that is not the case among most G-7 countries as well as those in southern Europe. Yet again, the East Asian NICs perform better than the G-7 block on average. Thus, as one might expect, the OECD as a whole, and the G-7 in particular, perform much worse on 'legal' corruption measures of corporate ethics than on the illegal ones. Surely one clear illustration of this is the continuing strong pressure in rich countries to protect trade, with disastrous effects on emerging economies.

Some clear conclusions can be drawn from evidence that governance and corruption constitute major constraints to development, investment and competitiveness. First, any remnants of skepticism over the desirability and feasibility of measurement of governance and corruption in both rich and poor countries seems unjustified. Transparency is key to improving governance and competetiveness in general, and monitoring worldwide progress on (legal and illegal) corruption would result in more effective decision-making by investors and policy-makers, as well as holding the public sector and corporations engaged in influence peddling more accountable.

Second, for strong institutions to take hold, much more attention must be given to incentives for ethical practice, beyond voluntary codes, conventions, and legal fiats currently in place. The private sector needs to be much more involved in this challenge, since it can play a key role in enhancing governance in the private and public sectors. New transparency mechanisms can be particularly effective, such as the extension to international organizations of the public delisting practice of the World Bank vis-a-

vis firms that have been found to cheat in Bank-funded projects.

And finally, and more broadly, the G-7 needs to catapult governance and anti-corruption as a top priority in their collective agenda. Not only because they face some considerable governance challenges of their own, but due to the increasing global evidence of the links between governance, development and global security.

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These are the authors' views, which do not necessarily reflect the views of their respective institutions.