Chapter 19

Corruption

Development Economics

S P E A

ASIA-PACIFIC HUMAN DEVELOPMENT REPORT

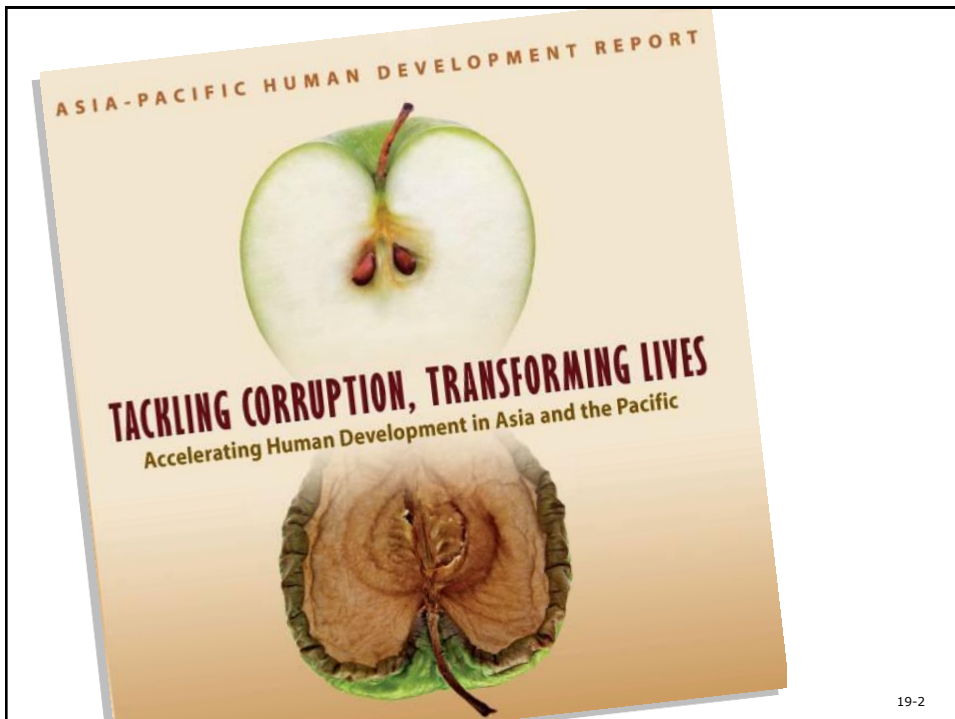TACKLING CORRUPTION, TRANSFORMING LIVES

Accelerating Human Development in Asia and the Pacific
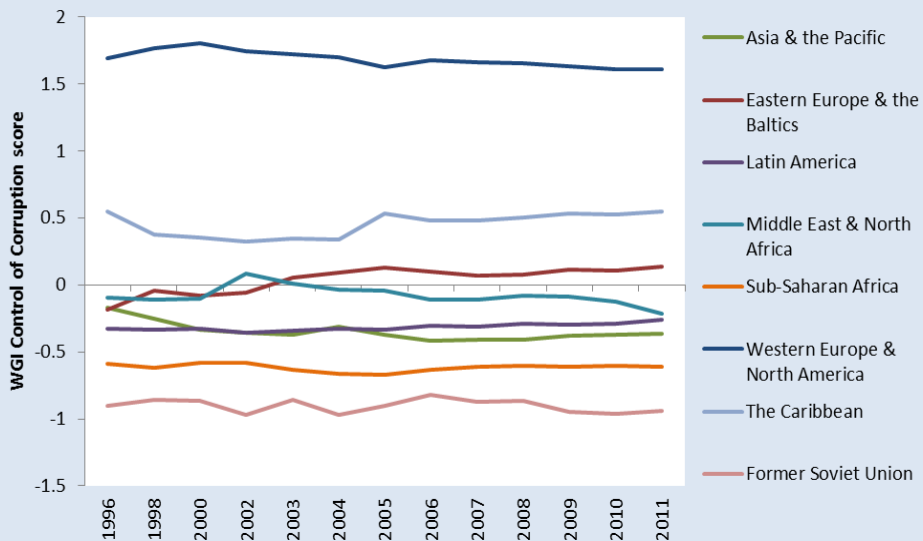
Three basic questions?

- What is the level corruption around the world?
- What is corruption?
- What are main types of corruption?

Evolution of the WGI Control of Corruption Average by Region (1996-2011)

Legend:
- Asia & the Pacific
- Eastern Europe & the Baltics
- Latin America
- Middle East & North Africa
- Sub-Saharan Africa
- Western Europe & North America
- The Caribbean
- Former Soviet Union

Y-axis: WGI Control of Corruption score

What is corruption?

What is corruption?

Misuse of public power
for private gain

Types of corruption

Types of corruption

- **Grand corruption –** involves **large sums**, (e.g. in massive contracts, and generally **high-level politicians** or officials)

- **Petty corruption –** involves **smaller sums**, (e.g., 'speed money' to **lower-level officials** to issue licenses)
  - Petty corruption is a misnomer. **Dollar amounts** may be **small**, but the **demands are incessant**, the number of **people affected enormous** and the **share of incomes** it eats up of the poor high

- **State capture –** is less understood by the public or the media
  - When companies pay public officials to shape laws, policies and regulations to their advantage, regardless of public good

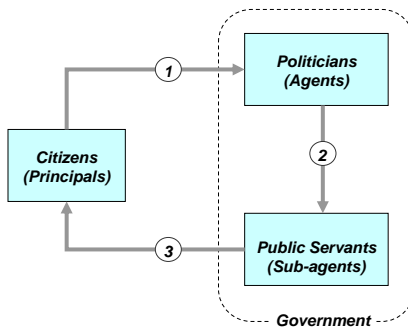**Not limited to governments**: commonly seen in the grey area of interactions between **public** and **private sectors**

For every '**taker**' there is a '**giver**'

Three conceptual questions

- How does corruption arise?
- How does corruption affect development?
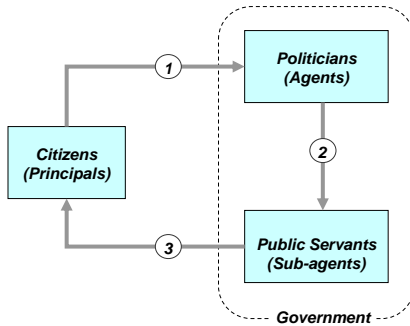- Why poor countries are trapped in corruption?

Question 1. How does corruption arise?

1. Principal-Agent Relationship
2. Divergent interests: politicians and/or public servants follow their own interests at the expense of citizens' interests
3. Information asymmetry: Weak institutions that do not allow monitor/control of citizens over politicians, and of politicians over public servants
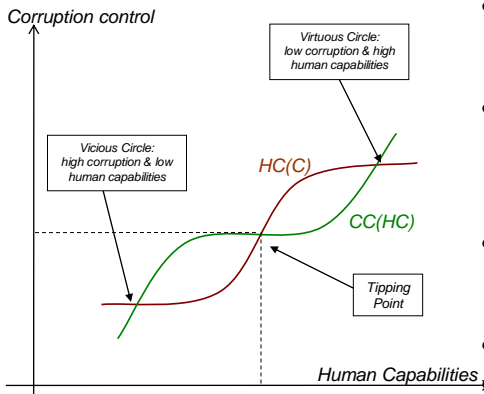
Q 2: What is the corruption - human development relationship?

- Arrow 1 shows the effect of HD on corruption
- Arrow 3 shows the effect of corruption on HD
- This two-way relationship creates either a vicious or a virtuous circle

19-11

Q 3: Why many poor countries are trapped in corruption?

- The Red Curve indicates the effect of Human Capacity on Corruption Control.
- The Green Curve indicates the reverse effect of CC on HC. Both curves are S-shaped.
- As a result, the intersections of the two curves create two steady states (equilibria).
- Two reform options
- The *tipping point* separates successful reforms from unsuccessful ones.
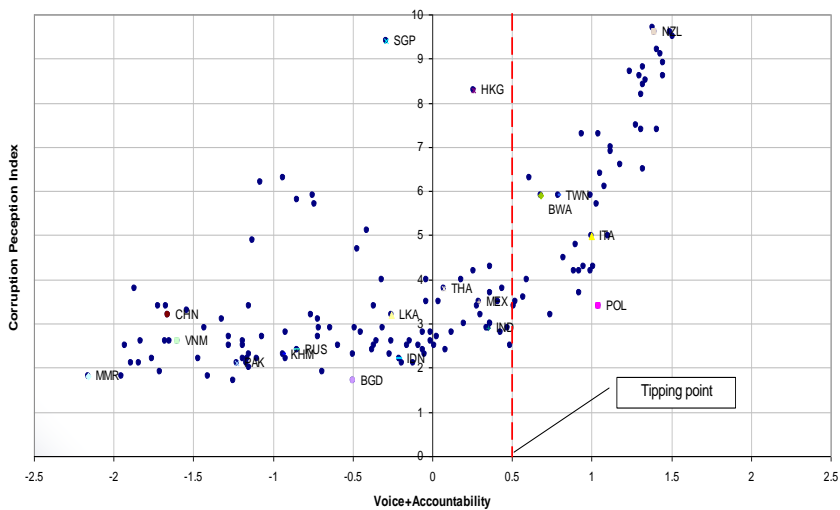
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One practical question
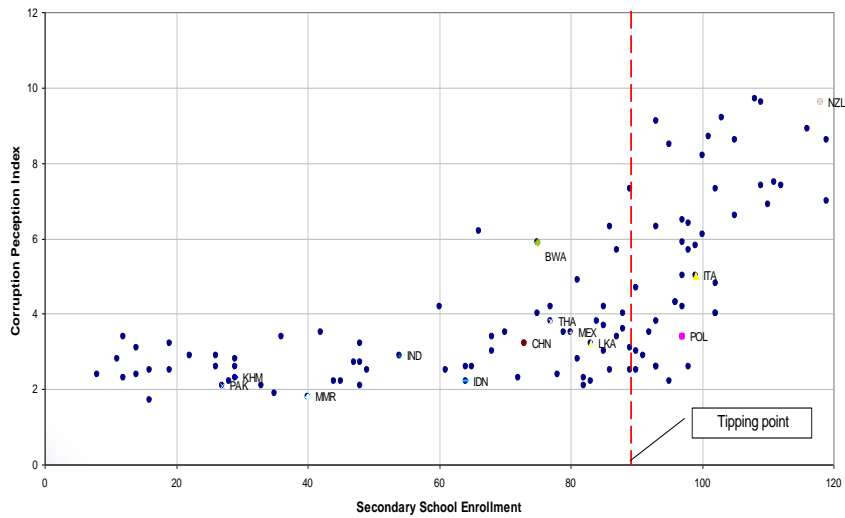
• How to get out of corruption?

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International path out of corruption (1)

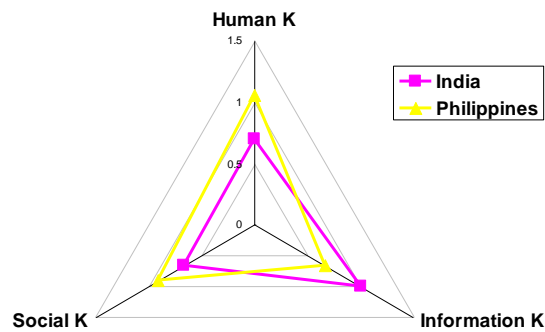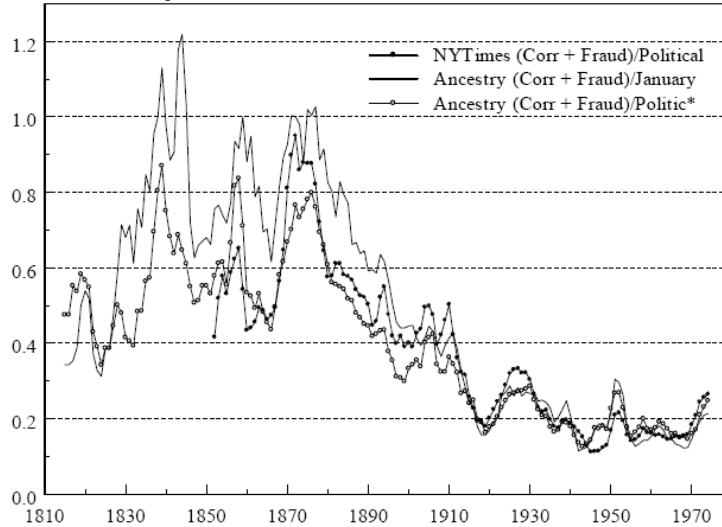19-14

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International path out of corruption (2)

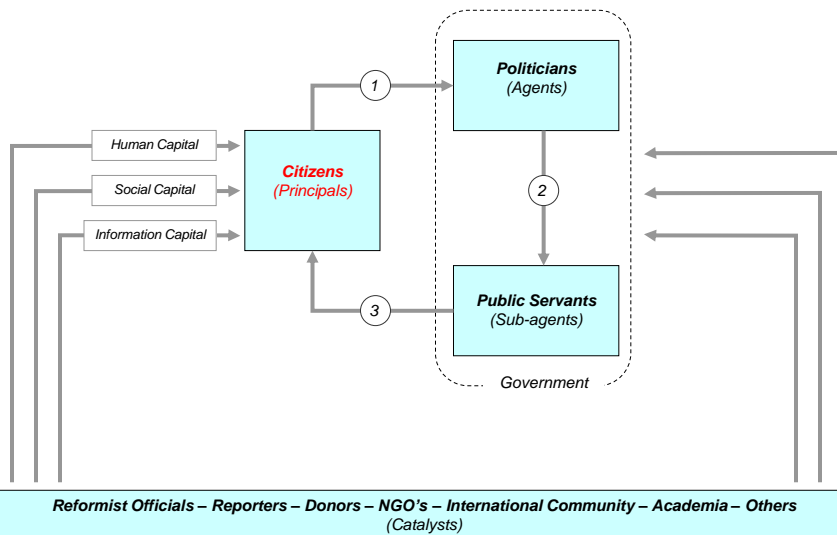# Human capabilities to fight corruption

The struggle against corruption in the US
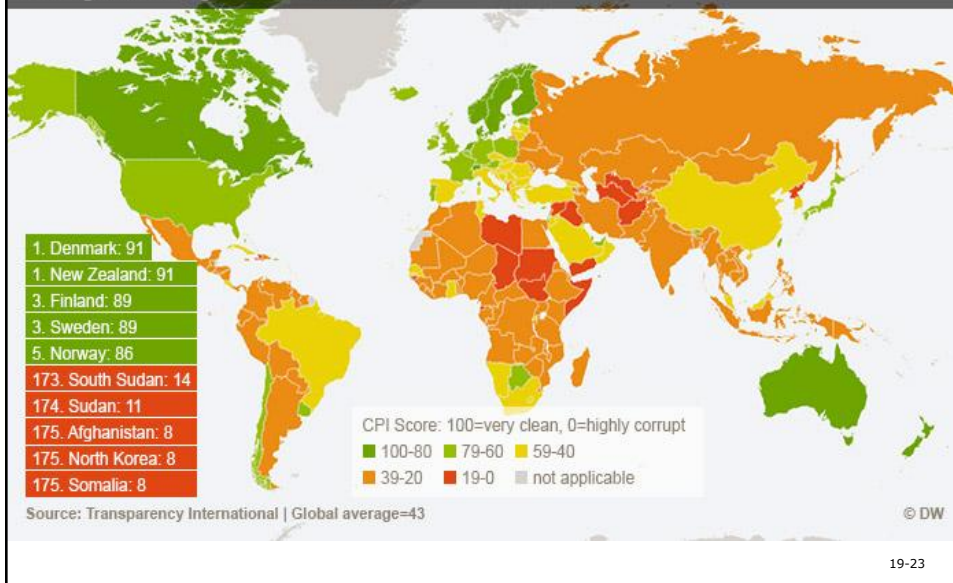
Index of Corruption and Fraud

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The human-capability approach to combating corruption

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WHAT IS CORRUPTION?

Corruption Perceptions Index 2013

1. Denmark: 91
1. New Zealand: 91
3. Finland: 89
3. Sweden: 89
5. Norway: 86
173. South Sudan: 14
174. Sudan: 11
175. Afghanistan: 8
175. North Korea: 8
175. Somalia: 8

CPI Score: 100=very clean, 0=highly corrupt
- 100-80
- 79-60
- 59-40
- 39-20
- 19-0
- not applicable

Source: Transparency International | Global average=43   © DW

GREASING THE WHEELS OR ROTTING THE FRUIT BASKET?

- Corruption and Development: *Two Views*

- *Positive effects of corruption on efficiency*: bribes help to break down bureaucratic walls and other obstacles to efficient exchange
  - Corruption seen as breaking the rules that prevent efficient bargaining (greasing the wheels or Coasian bargaining)

- *Negative effects*: contracts that cannot be enforced lead to substantial *hold-up and commitment* problems
  - Since bargaining power concentrated in hands of politician, their *behavior and demands become arbitrary*
  - *Lack of transparency* and certainty *erodes confidence and effectiveness of existing legal, economic, and political institutions*, formal and informal. Corruption spreads

- Especially with recent thought on the importance of institutions to development, the *consensus of opinion* has moved toward the *damaging view of corruption.*

WHY ARE SOME COUNTRIES MORE CORRUPT?

- Countries with *low levels of GDP per capita* tend to have *higher levels of corruption*.

- Treisman (Table 19.1) shows this strong correlation has held through time. Countries that *developed early* seem to have lower corruption scores.

- *Causation:* Does poverty breed corruption or is corruption just bad for development? Or are there *other factors* which explain both?

- There is also a *strong relationship* between *political institutions and corruption* (e.g., countries with democratic institutions and freedom of the press tend to be less corrupt).

- Panizza et. al. found that democracies with *elected presidents* tend to be more corrupt than parliamentary democracies, though the effect appears to influenced by Latin American history.

- *Electoral rules can be important*. Closed-list and proportional systems encourage more corruption than open-list rules.

WHY ARE SOME COUNTRIES MORE CORRUPT?

Table 19.1. Correlation of 2005 Perceived Control of Corruption and Maddison's Estimates of GDP Per Capita, 1500-1950.

|	1500	1600	1700	1820	1900	1950
World Bank control of corruption 2005	−0.47	0.145	0.228	.599[**]	.791[**]	.441[**]
p-value	.835	.52	.308	.000	.000	.000
Number of countries	22	22	22	46	42	146

There is a correlation between corruption in 2005 and the level of development in 1950, 1900, and even as far back as 1820. Countries that were richer in 1820 are less corrupt today. Note that ** indicates significant at the 1% level.

Source: Daniel Treisman, "What Have We Learned about the Causes of Corruption from Ten Years of Cross-National Empirical Research?" *Annual Review of Political Science* 10 (2007): 211–244.

CULTURE AND CORRUPTION

Figure 19.2. Parking Violations and the Corruption Index.
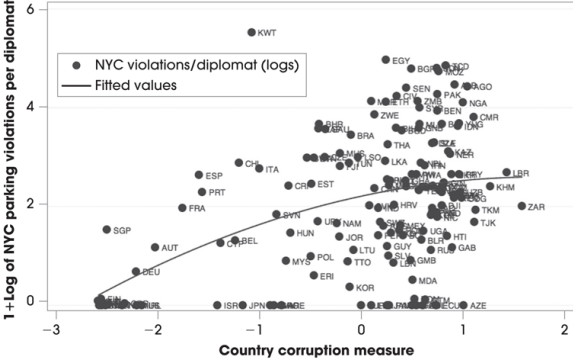
The horizontal axis measures country corruption and is derived from the World Bank corruption data described above. Here though, a higher score means more corruption. The vertical axis measures the log of (1+ a country's annual-per-diplomat New York City parking violations).

Source: Ray Fisman and Edward Miguel, "Corruption, Norms, and Legal Enforcement: Evidence from Diplomatic Parking Tickets," *Journal of Political Economy* 115, no. 6 (2007): 1038. Printed with permission from University of Chicago Press.