

Does Corruption Matter?

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Abstract

Corruption is a matter for both developed and developing countries as it restricts economic growth that is crucial for poverty alleviation and retards poverty reduction processes through increasing income inequality. This research essay will provide a cost-benefit analysis to support the above statement. The benefits that are gained by voters through corruption, are not well-distributed as different elite groups benefit the most from scarce resources and the net benefit of elite classes, bureaucrats and politicians are the net losses of poor citizens. Therefore, the benefits that corruption can bring, is a matter for poor citizens as corruption creates economic, social and political costs for them. Corruption reduces GDP growth and imposes a tax on FDI and these are crucial for developing and transitional economies. In addition, it restricts poverty alleviation by limiting job opportunities for poor.

Keywords: restrict, cost-benefit analysis ,scarce, reduce, crucial, limit, impose

1. Introduction

Globally, corruption costs around \$2.6 trillion annually, which is around 5% of the global GDP(Transparency International [TI] 2013,p.1). Corruption is an evil phenomenon both in wealthy and poor countries. For example, the United States of America (USA) lost \$600 billion in 2002 due to fraud cases only (Sarah 2008). In addition, the USA loses 5-10% of its annual budget due to corruption only in two programs, including Medicare and Medicaid (Global corruption report 2006).Furthermore, a study by Asian Development Bank (ADB 2008) found that bribery in public procurement costs \$1-\$2 trillion every year globally. Corrupt practices in this sector compels governments in Asian countries to spend 20 to 30% more and European Union(EU) \$160 billion annually, is marginally less than EU's entire budget. Moreover, TI(2013) reveals that 20 to 40% of all foreign aid is stolen every year due to corruption, largely by high levels of the bureaucrats and politicians.

Corruption also impacts severely upon developing countries by skewing money that could be invested on social sectors such as education and health (Francis 2003). For example, Bangladesh is one of the poorest, as well as one of the most corrupt countries in the world, losing 1.5% of its GDP and 8.4% of its national budget every year due to corruption(Transparency International Bangladesh[TIB] 2012). Another example is Columbia, who has to pay more than \$2 million for corruption in 32 public hospitals - an amount that could cover health insurance for 24,000 people (TI 2014).Furthermore, the World Bank cancelled \$1.2 billion of investment on the Padma Bridge in Bangladesh due to a corruption conspiracy. Around 30 million people could have benefited directly and improved the GDP by 1.2%, if the bridge had been built(The Daily Star 2013).

To conclude from the above discussion, corruption is a matter for both developed and developing countries. However, the cost of corruption is comparatively high in developing and transitional economies, as it works as a double-edge sword. On the one hand, it restricts economic growth that is

crucial for poverty alleviation. On the other, it restricts poverty reduction processes through increasing income inequality. This research essay will provide a cost-benefit analysis to support the above statement. Firstly, the essay will define corruption. Subsequently, the benefits of corruption will be addressed. Then the costs will be discussed from an economic, social, political and international perspective. Finally, a conclusion will assert that corruption is a matter of concern specifically for poor countries where people are dying in the vicious cycle of poverty; a condition that is perpetuated due to nourishing corruption.

Defining corruption:

Conventionally, corruption has two forms: one is economic and the other is political. Economic corruption refers to the use of public power for private gain, where the public officials are entrusted with some tasks by the elected political leaders. Civil servants try to create malfeasance for private gain that is difficult to monitor by the politicians (Bardhan 1997). Political corruption is the violation of rules and regulation that govern the distribution of public resources by the public officials and elected leaders to gain financial benefits or political support(Nye 1967).

Generally, corruption has different forms. Some widely used and useful types include:

- Petty corruption- exercised by civil servants who are comparatively honest, but are under paid. They practice it for their basic survival needs.
- Grand corruption- occurs in the high levels of the bureaucrats and politicians for personal gain. Foreign donor-financed projects or public procurement are the main sources of such corruption.
- Episodic corruption- corruption is not tolerated, dishonest officials are disciplined and caught.
- Systematic corruption- ways of malfeasance increase up from the dishonest collection points, and systems rely on corruption for their endurance.

Among the above types, systematic corruption pervades the whole society, bribery is routine and common in all transactions. Such entrenched corruption negatively affects the institutions, as well as individual behaviour, in all political and socio economic structures (Johnson 1996). Weak democratic culture, uneven distribution of wealth, weak civil society and a lack of institutional mechanisms often fail to challenge this problem, and exacerbate the overall impact of corruption in the country and in society (Robinson 2004). Therefore, corruption has severe economic, social and political impact specifically on developing countries. However, it has some benefits also. The next section is going to highlight some benefits that corruption brings, though these are debateable.

The benefits of corruption:

Economic scientists describe corruption as ‘sand in the gears of the economy’, while political scientists view it as ‘grease in the wheels of economy’ – a feature that makes the bureaucracy stronger in terms of their exercise of power and creates patron-client relationships between bureaucrats and citizens(Merton 1957). In addition, Leys(1989) advises that corruption is not always bad as higher-level corruption, in which there can perhaps be greater harmony between corruptor and corruptee. Furthermore, Becquart-Leclerq (1989) suggests that corruption makes strong relationships between the elite and parties, and ensures that power that is exercised, is strong. However, corruption is most effective under effective authoritarian governments in highly regulated markets, and becomes dysfunctional under strong democracies (Khan 1998).For example, South Korea and China’s economies boomed despite widespread corruption, and both countries have highly regulated economies and authoritarian governments (Khan1998). Therefore, speed money (bribery) works as grease in the economy that fosters market efficiently.

Bribery can ease bureaucratic rules and can assist markets to work properly. Osterfield (1992) argues that bribery works as speed money, correcting the market because public rules and laws have been formulated in that way, bureaucrats or elected leaders enjoy wide discretionary powers and put the price of goods and services above the market value. Speed money puts a price for discretionary powers and removes the

demand and supply gap between service providers and service seekers. Cuervo-Cazurro (2008) and Lui (1985) also found that corruption can ease transactions and speed-up bureaucratic procedures. This in turn can enhance the efficiency of civil servants. Furthermore, Nye(1967) suggests that corruption assists to grow middle and elite classes in a society, which assist entrepreneurs to flourish. Entrepreneurial activity flourishes under corruption in highly regulated economies(Dreher and Gassebner 2007). In addition, Mauro(1995) suggests that corruption can foster economic growth in two ways. It can work as speed money, permitting individuals to avoid bureaucratic delays, and also as economic motivation for government officials to work harder and more efficiently. So, corruption has positive impact on bureaucracy and economic progress.

Based on the above research, Melo and Quin(2015) suggest that if corruption can foster transactions and grease the wheels of the economy, then it can probably enhance political development in some societies. Nye (1967) also confirms that corruption can foster political development. However, Manzetti and Wilson(2007) argue that public institutions become weak under corruption, although voters in these countries support corrupt leaders because they have an expectation that they will receive tangible benefits. Nevertheless, the benefits that are gained by voters are not well-distributed. Different elite groups such the business community and lobbying groups benefit the most from scarce resources and the net benefit of elite classes, bureaucrats and politicians are the net losses of poor citizens. Therefore, the benefits that corruption can bring, is a matter for poor citizens as corruption creates economic, social and political costs for them. The next discussion is going to measure the costs of corruption.

2. The Costs of Corruption

The cost of corruption, varies from one group to another within a country, and also globally. Because bureaucrats might be pleased with the presence of corruption, the middle classes can enjoy illegal income and politicians can gain opportunities to make a fortune by stealing money from the public coffers. However, business groups can be affected as speed money raises the cost of goods and services. In addition, international economic agencies can be in trouble as corruption jeopardises the credibility of donor-funded programs. Furthermore, corruption can adversely affect the interest of the poor, whether corruption is petty or grand. Due to corruption, politicians, bureaucrats and wealthy sections in society win. However, the poor and marginalised as a whole lose. Therefore, corruption is associated with a large number of costs with regard to economic, social, political and international perspectives. As the volume of economic and social costs is huge and interrelated, this essay is going to focus on these two together, and will also focus briefly on political and international perspectives.

Economic and Social perspectives:

Corruption and poverty are interrelated. Though there is no conclusive study that concludes that corruption creates poverty or that poverty creates corruption. However, the general consensus is that the most corrupt countries in the world are the most poverty-stricken nations (Cullen 2008). For example, Bangladesh, which has notoriously ranked three times as the most corrupt country in the world, is one of the poorest nations, in which 20 % of its people live on less than \$1 a day(TIB 2012). In Africa, 340 million people or 50 % of the entire population live on \$1 a day in spite of being rich in natural resources (Cullen 2008). In addition, Asia is a continent of impressive economic growth; however, there is a high number of poor people who also live there. Furthermore, TI's Corruption Perception Index (CPI) 2012, that conducted a survey among 176 countries and graded them on a scale where 0 is the least corrupt and 100 is the highest corrupt country. On the scale, the bottom 50 countries were from developing world and no developed countries were on the bottom line. So, it can be assumed that corruption creates poverty or nourishes it, significantly in developing countries.

Interestingly, a study by Cullen(2008) found that, approximately \$197 billion was siphoned from the 48 poorest countries from 1990-2008 into the developed world or the Swiss Bank, mostly from Africa(69%),

followed by Asia(29%). The rulers of Nigeria siphoned around \$500 billion, equivalent to the total amount of Western aid to African countries over the last 40 years. Furthermore, three dictators from Latin American countries, Peron, Perez Jimenez and Batista, drained around \$1.5 billion from their countries and deposited it in the Swiss Bank(Nye 1967). Furthermore, Bangladesh is one of the poorest countries, has ranked as one of the highest depositors in the Swiss Bank (The Daily Star 2014).The idle capital deposited in the Swiss Bank is a net loss for developing countries, as the deposited money could be invested to create more sources of income for poor people(Nye 1967). If US \$100 million is enough for the full immunization of 4 million children in developing world, suggested by Cullen(2008), the question is how many hospitals, schools or AIDs vaccines could be administered or spent on poverty alleviation and improve the livelihood of millions of people by investing the huge capital that takes away from these poorest countries. Therefore, it can be concluded that corruption is a very serious matter for poor, as it creates poverty or restricts poverty alleviation, specifically in developing countries.

Public procurement and foreign aid are the two major sources of robbing capital from these countries. Globally, \$1-2 trillion is spent on bribery(both developed and developing countries) in the public procurement sector annually. In addition, since 60 years near \$1 trillion aid has been transferred in to Africa and 70% of total aid has been linked to widespread corruption (The Wall Street Journal 2009). Furthermore, substandard goods and services are one of the direct consequences of rampant corruption in public procurement. The poor mainly bear the burden of these substandard products as faulty roads or infrastructures cost millions of lives. For example, devastating earthquakes that caused a high death toll in China in 2008, Haiti in 2010 and India 2001, were blamed for corruption in constructing public buildings(ADB 2008).

Corruption in public procurement not only takes away millions of lives of poor, but also restricts poverty alleviation process as politicians prefer to invest in more capital intensive projects than labour intensive ones (Rose-ackerman 1999). This biased investment strategy deprives the poor from income opportunities. A study by Gupta et al(2002), found that if corruption increases one %age point, it would reduce income generating activities for the poor by 5%. As a result, the poor has little opportunity to income and again find themselves trapped in a vicious cycle of poverty (Gupta et al 2002). Therefore, poor are the worst victims of widespread corruption in public procurement and foreign aid.

A higher rate of corruption is associated with a higher shadow economy, and lower GDP growth. A study by Buehn and Schneider(2012) that looked at 52 countries, both developed and emerging between 2000-2005, confirmed the above statement. Friedman et al(2000) also found that a high degree of corruption encourages underground businesses and the government is deprived of tax and this makes government less effective. For example, a study by Mauro(1997b) on over 100 countries between 1982-1995, found that if corruption increased 2%age points, it would decrease the GDP by 0.5 % and investment would decrease by 4 %. In addition, Tanzi and Davoodi(1997) asserted that a 2 per cent increase in corruption also decreases 0.5 % of public investment on education. Furthermore, another study by De Maria(2008) found that corruption costs more than \$148 billion annually in African economies, which translates to a fifty % loss in tax revenue, an increase of 20 % in goods and services, and a 25 % loss of Africa's GDP. So, corruption is associated with lower public investment and slower economic growth in Africa and other rising economies.

A higher level of corruption is associated with a lower level of FDI. Corruption acts like a tax on FDI. For example, the tax rate of Singapore, known as one of the least corrupt countries, will increase by 20 % on FDI if the corruption level goes to that of Mexico (Ampratwum 2008). However, Mauro(1995) disagrees with this statement and argues that a huge volume of FDI flows in South Korea and China, despite widespread corruption in these places. However, these countries might draw more FDI if the corruption level was lowered(Rose-Ackerman1999). Nevertheless, ACRC(2013) suggests that the volume of FDI is 5 % less in corrupt countries than to comparatively clean countries. Therefore, FDI, that is crucial for developing countries for sustaining economic growth, is also impacted by corruption.

3. Political perspective

Political Corruption is about more than just influencing trade or favouring contracts. It weakens political institutions and influences party financing from illegal sources. Weak political institutions can undermine democracy that restricts citizens from exercising their legitimate rights that result in motivating political parties for vote-buying. For example, a study by the Anti-Corruption Resource Centre (ACRC 2013) found that a minor ruling party in Brazil in 2005 was accused of buying votes from major parties in order to sustain political support and loyalty. The ruling parties were providing around \$12,500 every month to every parliamentarian. The above example exemplifies that political corruption is not just robbing money alone; it also poisons politics and devastates democracy as it distorts democratic practices of public institutions and political parties. It destroys people's faith in politics and also increases distrust among citizens, politicians and parties when policy makers largely involve in organised crime and illicit acts.

Political corruption contains various forms of crime and illicit acts, like trafficking, drugs or armed business. For example, a study by TIB(2012,p.8) on lawmakers in the Parliament of Bangladesh, found that among 300 law-makers, 97 % of them were involved in corrupt practices while 70 % were involved in criminal activities like killing, land grabbing and extortion of public tenders. Another example is, the South African Arms deal scam. Jacob Zuma, deputy president of South Africa, was accused of taking bribes from an Arms company for immunity in an investigation and providing performance support (ACRC 2013). Furthermore, political corruption not only ruins the state apparatus but also affects the media, a watch dog of democracy. The media becomes branded as biased, as the major political parties try to buy or influence the media for political coverage. For example, media owners in Guatemala and Uruguay have achieved significant political favour from political parties by offering them free airtime. Furthermore, Silvio Berlusconi, Premier of Italy, is the largest owner of three private broadcasters and has control of three public networks. However, the media played a significant role in uncovering corruption on "Padma Bridge" issue, when the World Bank cancelled the \$1.2 billion finance project and Anti-corruption Commission(ACC), the highest authority for curbing corruption in Bangladesh, failed to investigate the allegations neutrally. Therefore, it can be concluded that political corruption not only devastates state apparatus but also is associated with organised crime or illicit acts that substantially a grave concern in international perspective also.

4. International perspective

International donors and finance agencies have committed to show zero tolerance against corruption as foreign aid fails to get to the intended beneficiaries. A substantial amount of aid has been stolen from recipient countries (TI 2013). However, the most corrupt countries are getting the highest volume of foreign aid and a substantial amount of this aid is being absorbed by elected politicians and public officials .For example, Somalia and Afghanistan were respectively the first and second highest recipients of United Kingdom(UK)'s aid in 2012, though these countries have been branded as the most corrupts(The Telegraph 2014). Another example is drug trafficking. Global opium market largely depends on Afghanistan, Myanmar and organised criminals use different routes in cross borders like Eastern Europe, South Western Europe , South Asia, middle Asia. Large numbers of the countries in the world have been affected by organised crime due to nourishing corruption specifically in public sector(United Nations Office on Drugs and Crime 2014). Therefore, organised crime is increasing. In addition, organised crimes within and beyond the countries destabilize human rights, law and order, result in civil or political unrest. These illegal activities also affect comparatively clean country's foreign investment or international business or aid intended to poverty alleviation and other development purposes.

5. Conclusion

From the above cost-benefit analysis, it can be concluded that the costs that are generated through corruption is a serious matter for a developing country's economic and social, political perspectives. Though it costs severely developed countries also, however, the cost of corruption is significantly high in developing and transitional economies. Corruption reduces GDP growth and imposes a tax on FDI and these are crucial for these economies. In addition, it restricts poverty alleviation by limiting job opportunities for poor. Furthermore, it weakens democracy, public institutions, rule of law, result in weak state. However, grand corruption in public procurement is not only a serious matter for developing or developed countries but also for international business firms and aid agencies. Because, corruption restricts competition, increases cost of production, result in efficiency and low quality of goods and services. Though bureaucrats for personal gain, growing middle classes might be benefited through corruption. However, bureaucracy as an institution, can be devastated entirely that also poisons politics and state apparatus. International donors also consider it as a serious matter due to the devastating effect of corruption on foreign aid that could be invested for poverty alleviation and other development purposes. Furthermore, if \$500 billion that was robbed from Nigeria could be invested in education and health, or the money that was received from foreign aid by Bangladesh, this would help the poor more efficiently (Cullen 2008). Therefore, corruption is a great concern for developing and transitional economies where every day thousands of people enter into poverty and a substantial number of them die every day due to poverty-related causes.

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