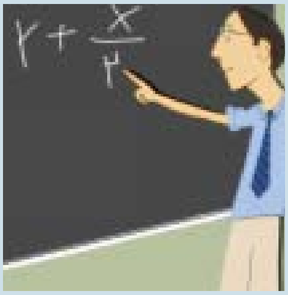

10 Myths About Governance and Corruption

Daniel Kaufmann

GOVERNANCE—which remains a sensitive and misunderstood topic—is now being given a higher priority in development circles. A few donors and international financial institutions (IFIs) have begun to work with some emerging economies to help reduce corruption, and encourage citizen voice, gender equality, and accountability. When the Group of Eight countries announced in July their decision to double aid and debt relief to the poorest countries in Africa, governance concerns were prominent. And in May, the joint report by the Africa Commission explicitly stated: "Good governance is the key . . . Unless there are improvements in capacity, accountability, and reducing corruption . . . other reforms will have only limited impact."

But is good governance and controlling corruption really so fundamental for development? The explosion of empirical research over the past decade, coupled with lessons from countries' own experience, have given us a more solid basis for judging the effect of governance on development, and the effectiveness—or lack thereof—of strategies to improve it. Yet there are still unresolved questions and debates in the development community, not only about the importance of governance, but also about the ability of IFIs to help countries improve on it. Let us therefore go back to basics and address some prevailing "myths" about governance and corruption.

Myth #1: Governance and anticorruption are one and the same. We define governance as the traditions and institutions by which authority in a country is exercised for the common good. This includes the process by which those in authority are selected, monitored, and replaced (the political dimension); the government's capacity to effectively manage its resources and implement sound policies (the economic dimension); and the respect of citizens and the state for the country's institutions (the institutional respect dimension). By contrast, corruption is defined more narrowly as the "abuse of public office for private gain."

Myth #2: Governance and corruption cannot be measured. It is true that less than a dozen years ago virtually no internationally comparable measures of governance or corruption existed. But in recent years, the World Bank and others have sought to remedy this. At the World Bank, we have constructed aggregate governance indicators that cover more than 200 countries, based on more than 350 variables obtained from dozens of institutions worldwide. Our indicators cover the following six dimensions of governance: voice and accountability; political stability and the absence of major violence and terror; government effectiveness; regulatory quality; rule of law; and control of corruption.

While the indicators represent a big step forward, there are measurement challenges. Margins of error are not trivial, and caution in interpreting the results is warranted—one should not precisely rank countries. But these margins of error have declined, and are now substantially lower than for any individual measure of corruption, governance, or the investment climate. As a result, the World Bank's governance indicators are used worldwide for monitoring performance, for country assessments, and for research.

Myth #3: The importance of governance and anticorruption is overrated. Thanks to these and other advances in empirical measurement, a number of researchers have examined the impact of governance on development. The research generally shows that countries can derive a very large "development dividend" from better governance. We estimate that a country that improves its governance from a relatively low level to an average level could almost triple the income per capita of its population in the long term, and similarly reduce infant mortality and illiteracy. Such a relative improvement (by one standard deviation) would correspond, for instance, to a move up in our ranking for the "control of corruption" dimension in our database, taking Equatorial Guinea to the level of Uganda, Uganda to Lithuania, Lithuania to Portugal, and Portugal to Finland.

Governance also matters for a country's competitiveness and for income distribution. In the case of corruption, research suggests it is equivalent to a major tax on foreign investors. In many developing countries, corruption represents a "regressive tax" on the household sector as well: lower income families pay a disproportionate share of their incomes in bribes to have access to public services (compared with higher income groups), and often end up with less access to such services because of corruption. A rough estimate of the extent of annual worldwide transactions that are tainted by corruption puts it close to $1 trillion.

To make matters worse, aid-funded projects tend to fail in corrupt settings. And corruption undermines fledgling democracies. Of course, governance is not the *only* thing that matters for development. Macroeconomic, trade, and sectoral policies are also important. But when governance is poor, policymaking in other areas is also compromised.

"The coupling of progress on improving voice and participation—including through freedom of expression and women's rights—with transparency reforms can be particularly effective."

Myth #4: Governance is a luxury that only rich countries can afford. Some claim that the link between governance and incomes does not mean that better governance boosts incomes, but the reverse—higher incomes automatically translate into better governance. However, our research does not support this claim. It is thus misleading to suggest that corruption is due to low incomes, and invent a rationale for discounting bad governance in poor countries. In fact, the evidence points to the causality being in the direction of better governance leading to higher economic growth. A number of emerging economies, including the Baltics, Botswana, Chile, and Slovenia, have shown that it is possible to reach high standards of governance without yet having joined the ranks of wealthy nations.

Myth #5: It takes generations for governance to improve. While it is true that institutions often change only gradually, in some countries there has been a sharp improvement in the short term. This defies the view that while governance may deteriorate quickly, improvements are always slow and incremental. For instance, there has been a significant improvement since 1996 in the "voice and accountability" indicator in countries ranging from Bosnia, Croatia, and Ghana, to Indonesia, Serbia, and Sierra Leone. And the improvements exhibited by some African countries in a short period of time challenge the "Afro-pessimists." Even so, it is sobering that, on average, there has not been a worldwide improvement in overall governance during this period—and in a number of countries, including the Ivory Coast, Nepal, and Zimbabwe, there has been a sharp deterioration.

Myth #6: Donors can "ringfence" projects in highly corrupt countries and sectors. With the possible exception of some humanitarian aid projects, the notion that the aid community can insulate projects from an overall corrupt environment in a country is not borne out by the evidence. The data suggest that when a systemic approach to governance, civil liberties, rule of law, and control of corruption is absent, the likelihood of an aid-funded project being successful is greatly reduced.

Myth #7: Fight corruption by fighting corruption. A fallacy promoted by some in the field of anticorruption, and at times also by the international community, is that one "fights corruption by fighting corruption"—through yet another anticorruption campaign, the creation of more "commissions" and ethics agencies, and the incessant drafting of new laws, decrees, and codes of conduct. Overall, such initiatives appear to have little impact, and are often politically expedient ways of reacting to pressures to do something about corruption, substituting for the need for fundamental and systemic governance reforms.

Myth # 8: The culprit is the public sector in developing countries. A common fallacy is to focus solely on the failings of the public sector. The reality is much more complex, since powerful private interests often exert undue influence in shaping public policy, institutions, and state legislation. In extreme cases, "oligarchs" capture state institutions. And many multinational corporations still bribe abroad, undermining public governance in emerging economies. There are also weaknesses in the nongovernmental sector. Further, traditional public sector management interventions have not worked because they have focused on technocratic "fixes," often done through technical assistance importing hardware, organizational templates, and experts from rich countries.

Myth #9: There is little countries can do to improve governance. Given the long list of interventions that have not worked, as well as the role often ascribed to historical and cultural factors in explaining governance, it is easy to fall into the pessimist camp. That would be a mistake. First, historical and cultural factors are far from deterministic—witness, for instance, the diverging paths in terms of governance of neighboring countries in the Southern Cone of Latin America, the Korean peninsula, the transition economies of Eastern Europe, and in Southern Africa. Second, there are strategies that offer particular promise. The coupling of progress on improving voice and participation—including through freedom of expression and women's rights—with transparency reforms (see box) can be particularly effective.

Toward a transparency reform scorecard

The data suggest that transparency helps improve governance and reduce corruption—essential ingredients for better development and faster economic growth. But there is a need for the development aid community to pay more attention to the issue. For that reason, at the World Bank Institute we have begun to construct an index to help make transparency more transparent. Further, in terms of reforms, a basic checklist, which countries may use for self-assessment, includes:

- public disclosure of assets and incomes of candidates running for public office, public officials, politicians, legislators, judges, and their dependents;
- public disclosure of political campaign contributions by individuals and firms, and of campaign expenditures;
- public disclosure of all parliamentary votes, draft legislation, and parliamentary debates;
- effective implementation of conflict of interest laws, separating business, politics, legislation, and public service, and adoption of a law governing lobbying;
- publicly blacklisting firms that have been shown to bribe in public procurement (as done by the World Bank); and "publish-what-you-pay" by multinationals working in extractive industries;
- effective implementation of freedom of information laws, with easy access for all to government information;
- freedom of the media (including the Internet);
- fiscal and public financial transparency of central and local budgets, adoption of the IMF's Reports on Standards and Codes framework for fiscal transparency, detailed government reporting of payments from multinationals in extractive industries, and open meetings involving the country's citizens;
- disclosure of actual ownership structure and financial status of domestic banks;
- transparent (web-based) competitive procurement;
- country governance and anticorruption diagnostics and public expenditure tracking surveys (such as those supported by the World Bank); and
- transparency programs at the city (and subnational) levels, including budgetary disclosure and open meetings.

Myth #10: There is not much the IFIs can do. Some development experts are skeptical about the ability of IFIs and donors to help countries improve their governance—either because of a conviction that "the 'macro' matters more," a mistaken belief in historical "determinism," or a view that the interventions needed to improve governance are politically sensitive and thus difficult for outsiders to encourage. Surely, there are areas that fall outside the mandate of IFIs, such as promotion of fair multiparty elections. But initiatives to encourage transparency, freedom of information and an independent media, participatory anticorruption programs led by the country, and gender equality—all of which have been underemphasized so far in the fight against corruption—may well be within the ability of IFIs and donors to do something about. Such initiatives, complemented by supporting targeted reform of highly vulnerable institutions (which often include procurement, tax, customs, or the judiciary) offer much promise.

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The challenge of governance and anticorruption confronting the world today strongly argues against the "business-as-usual" modus operandi. A bolder approach is needed, and collective responsibility at the global level is called for. The rich world must not only deliver on its aid and trade liberalization promises, it must also lead by example. OECD countries should ratify and effectively implement the 2003 UN convention against corruption, and take steps (as Switzerland is starting to do) to repatriate assets looted and stashed abroad by corrupt officials. And transnational corporations should refrain from bribery and support improving governance practices in host countries. As for the IFIs and donors, there is a need to grapple with questions of selectivity and effectiveness in aid programs, anchoring aid decisions within a governance prism and helping countries build capacity to effectively absorb aid. Improving transparency will be key. Finally, countries themselves must take the lead in improving governance. ■

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For more information about the World Bank's work on governance and access to the data, indicators, and diagnostics, visit http://www.worldbank.org/wbi/governance/