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Comments: Dani Rodrik and James E. Rauch

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The fascinating papers in part I of this book focus on the causes and consequences of corruption, primarily from a domestic perspective. We learn that corruption is a multifaceted and complex phenomenon, that it is often deeply rooted in the politics of a country, and that it is measurably costly in terms of foregone investment and growth opportunities as well as in terms of equity.

How we deal with corruption, however, depends very much on *why* we think it is a problem and which of its consequences we choose to deal with. The papers from this session tell us that corruption is first and foremost a domestic problem; that is, it is mostly the people of Indonesia, Haiti, or Zaire—to pick some nonrandom examples—who suffer from the presence of corrupt bureaucrats and leaders. The social price of corruption is largely paid in local currency by local people.

This is an important, if implicit, lesson because corruption owes its current salience as an international problem not primarily to a concern about what corruption does to the domestic economy and polity, but to a concern about what it does to foreign exporters and investors. Corrupt bureaucrats have always been around, and it seems unlikely that the problem somehow has become more acute in recent years. Rather, the developing countries in which these problems are rampant have now become more prominent on the radar screens of European and American businesspeople. Meanwhile, the Foreign Corrupt Practices Act

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(FCPA), which prohibits US-based companies from engaging in certain activities deemed corrupt while abroad, has put the United States at a competitive disadvantage relative to other industrial countries. Together, these two factors go a long way toward explaining why corruption has been transformed from an "economic development" problem into an "international trade and investment" problem. We in the industrial countries now care about corruption in the developing world because we believe "their" corruption hurts us.

One might say that the fact that people are paying more attention to this issue has to be a good thing. To some extent this is true. But I will be somewhat contrarian and argue that this shift in emphasis may have some unwelcome consequences if it is not complemented by efforts aimed at the deeper, developmental challenges posed by corruption.

The trouble with viewing corruption through the lens of international trade and investment rather than through the lens of development is that the issue becomes primarily one of redistribution—whether among the industrial countries or between industrial-country exporters and developing-country importers—and of confrontation. With this emphasis, the argument against corruption loses much of its efficiency rationale. Let me illustrate with a relevant example.

Suppose a developing country with a corrupt president invites bids for a large order of jet aircraft. Consider first the implications of the FCPA. Since the president and his entourage are determined to get a kickback, the Americans soon find themselves out of the running, and the Europeans get the order. But since the president now cannot play the Europeans off against the Americans, presumably his bribe (from the Europeans) is lower than what it would have been without the FCPA. Part of the cost of bribing the president, moreover, is presumably passed on in the final price of the European aircraft.

What are the implications of this from the perspective of global welfare? If the European jets are reasonably close substitutes for the American ones (which they are), the world as a whole is no worse off: whatever the Americans and the corrupt president lose, the Europeans gain, and the developed country still gets the same number of jets. A lot of money changes hands, but the global outcome is a wash and there is little or no efficiency loss.

Now consider what would happen if the Americans managed to get the Europeans on board and all exporters agreed to stop corrupt payments. Then the next time the developing country places an order for jet aircraft, the president does not get his bribe. His loss is the joint gain of the Europeans and the Americans. But if one assumes, as is likely, that there is no domestic manufacturing capability for the jets in the developing country, and that therefore the order has to be filled either by the Americans or by the Europeans, once again the world as a whole is no better off. The effects are purely redistributive.

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Finally, consider what would happen if the corrupt president were overthrown and a clean government took over. Since the European and American exporters have already sworn off paying bribes, they are no better off. They may in fact end up worse off if the new regime, lacking a personal profit motive in the transaction, decides to order fewer aircraft. The primary beneficiaries, of course, are the people of the developing country.

This example suggests a number of things. First and foremost, the primary economic concern raised by corruption at the *international* level is often a distributive concern rather than an efficiency concern. This puts corruption as a trade issue in the same category as, for example, trade-related intellectual property rights (TRIPs) during the Uruguay Round and makes it quite different from the bread-and-butter concerns of the GATT/WTO system, such as reducing trade barriers. The example also suggests that the statement that I suspect we will now hear too often, namely—that "corruption is a tax on foreign exporters and investors, and hence acts as a trade and investment barrier,"—is misleading. For one thing, corruption is nondiscriminatory in a trade sense, in that domestic as well as foreign transactions are subject to it. In addition, as the aircraft example highlights, corruption need not be distorting in the sense that it reduces economic efficiency.

If we still wish to address corruption as an international trade and investment issue, a more appropriate justification may be found in terms of the fairness and morality of the practices and procedures that govern international transactions. Practices that violate ethical norms held within at least one of the countries party to trade undermine the legitimacy of trade itself and erode confidence in markets. This is a perfectly sound basis for international concern. Fairness and morality are not things that economists talk much about, but we should not lose sight of the fact that the FCPA itself was motivated by post-Watergate ethical concerns and that many (if not most) US, European, and Japanese businesspeople would agree that they would rather not engage in practices considered ethically repugnant in their home countries. This may be the more solid argument for cracking down on corruption in international trade and investment.

However, an ethics-based approach to corruption as an international problem opens a Pandora's box of complications, some of which may well end up embarrassing the same US and European businesspeople now advocating strict international controls on corrupt practices. Once it becomes legitimate to criticize developing countries for behavior that offends industrial-country businesses, what is to prevent other groups in the industrial countries from broadening the scope of the discussion to include similar matters of concern to them? Think, for example, of labor standards. Countless governments have signed the relevant International Labor Organization (ILO) conventions on child labor yet fail to

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enforce them rigorously and therefore are violating domestic laws as well as international obligations. Is there any real difference, one might ask, between extending WTO authority to goods produced by child labor and extending it to corrupt trade practices? What is the difference between the United States imposing trade restrictions on countries with labor practices that would be considered odious in the United States and imposing sanctions on countries with rampant corruption? Yet how many businesspeople would feel comfortable with the extension of the WTO's mandate or the use of the Super 301 for provisions of US trade law to address concerns over labor standards? On both these matters, the opposition of the Republicans in Congress leaves little doubt as to where the US business community stands.

I choose labor standards only as an example. A similar analogy can be drawn with respect to trade with highly repressive, authoritarian regimes. How many industrial-country businesspeople would want their own countries' trade policy (or the WTO) to meddle with trade and investment flows on the grounds that some political regimes deny civil and political rights to their citizens?

To recapitulate, I am as much against corruption as the next person. But I think corruption is a developmental problem, not a trade problem. The way to deal with it is through improved governance and better incentives in the developing countries themselves. I am all for corporate codes of conduct and legislation such as the FCPA that prevent home-country firms from partaking in corrupt practices wherever they do business. To the extent that international involvement is likely to be helpful, it is agencies such as the World Bank and bilateral aid groups that can and should make a difference.

But when I hear that corruption may be an agenda item for the next WTO ministerial meeting, or when the US trade representative starts talking of corruption as an unfair trade practice that could cost US companies $40 billion in foregone revenues, I become nervous. I fear that what drives these new demands is a battle for market shares rather than a genuine concern for global welfare. I worry that we will begin to confuse the huge developmental problem that corruption truly is with the problems that corruption causes for international commerce and that we will start to use the former as an excuse for the kind of trade initiatives I have just cited. The risk in viewing corruption through the lens of international trade and investment, in my view, is that doing so diverts attention from the serious issues raised in this book and turns the debate into an us-versus-them conflict between the industrial and the developing world. And I fear that this is much less likely to prove productive toward the ultimate goal of fighting corruption.

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JAMES E. RAUCH

I will take as my point of departure Susan Rose-Ackerman's paper (chapter 2), although some of what I have to say will be closely related to the quantitative work of Paolo Mauro (chapter 4). I will first discuss bribery in the awarding of government contracts and then discuss my own research on the influence of bureaucratic career paths on bureaucratic corruption more generally.

Bribery in Awarding of Government Contracts

Bribery, or influence peddling, in the awarding of government contracts is common even in the most advanced industrial countries. There is often a fuzzy line between illegal bribery and legal political contributions. In the country with which I am most familiar, the United States, incidents of choosing contractors on the basis of campaign contributions (usually legal) can be observed all the way from municipalities up to the federal government.[1] A related form of influence peddling that does not involve bribery is the "revolving door" phenomenon, in which government officials leave office and join private firms that then bid on contracts from the government agencies for which the officials formerly worked. In the United States this practice is considered potentially corrupting, and laws attempting to control it include a "lifetime ban on all former executive branch employees from lobbying on matters in which they were 'personally and substantially involved' while in office" and "a two-year ban on matters that were 'under their official responsibility within the year preceding termination of government service'" (Congressional Quarterly 1991, 812). In Japan, on the other hand, the revolving door is virtually institutionalized, where it is known as *amakudari*, or "descent from Heaven." In the wake of threatened bank failures and financial scandals, however, the attitude in Japan has become more similar to that in the United States: "There is already a restriction preventing bureaucrats from taking jobs in such companies [that they used to regulate] until two years after their retirement. But some in the Finance

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1. The US Supreme Court recently ruled, however, that punishing independent contractors by revoking their contracts for failing to show political loyalty (e.g., by giving a campaign contribution to the other candidate) is a violation of their right to free speech. Justice Antonin Scalia dissented from the ruling, arguing that political favoritism is well-entrenched in American life and should not be ruled unconstitutional (*Washington Post*, 29 June 1996, A1).

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Ministry have proposed making that five years" (*New York Times*, 5 May 1996, section 1, 8).

I would argue that, in general, this kind of influence peddling, whether through bribery or the revolving door, is often functional—and is extremely difficult to control in any case and thus should perhaps not be the main focus of anticorruption efforts. But in some cases influence peddling is not functional, and I would argue that reform should be aimed at deterring these cases.

The following anecdote, which concerns *private* business practices in Japan, illustrates my thesis. The entrepreneur of a small Japanese firm was convinced he had a superior input for the production of a large Japanese firm, but he was having trouble getting the attention of that firm's purchasing manager. He therefore sent a gift (the kind that comes in a box, not cash) and an invitation to dinner. The purchasing manager accepted, and over dinner the entrepreneur was able to explain the virtues of his product and win the contract.

Why do we observe this type of business practice? I believe that the incomplete and inadequate information provided by prices for differentiated products or services is a major cause. When a reputable producer of a simple commodity such as aluminum seeks new customers, all it has to do is offer a lower price than what the prospective customers are currently paying: the customers will either switch or demand that their current supplier meet the lower price. But when the item for sale is a sophisticated sewing machine for a garment factory, a cheaper price tells the buyer little. How does the new sewing machine compare with the model already on the shop floor? At a minimum, the buyer needs to see a sample and a demonstration, and probably not only the purchasing manager but also the production managers or engineers have to see it and must form an opinion on whether to buy. The buyer may judge that the expected payoff is not worth the trouble of even considering the new product. In such circumstances, a "gift" can tip the balance, making the effort to obtain the information worth the buyer's while.

Many of the things that governments buy, such as infrastructure projects and weapons systems, are likewise highly differentiated products for which the responsible bureaucrat cannot simply accept the lowest bid. How then does the bureaucrat choose? In the case of the revolving door, the contract often goes to the bidder whose capabilities the bureaucrat knows and trusts from their period of common government service. If the bureaucrat in question is an elected official, he may also have come to know and trust the bidder's capabilities through the access the latter has previously obtained in return for a campaign contribution.

This system of bribes as "access charges" ceases to be functional when corrupt favoritism leads to nonperformance—the bridge falls down or the plane does not fly. But then the problem is the nonperformance rather than favoritism. The appropriate reform may be to tie officials'

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pay and career advancement to the performance of the contracts they award. (Indeed, if officials are indifferent to performance, this is a problem whether or not they take bribes.) Putting such an incentive structure in place might not be as straightforward as it sounds, but it would surely be easier than trying to deter bribery-induced favoritism, which can be concealed in myriad ways. One avoids more welfare loss with less effort.

Bureaucratic Career Paths

The career paths that bureaucrats face may be an important determinant of whether they become corrupt. Rose-Ackerman makes the important point that "higher-ups are likely to have greater freedom to create extra rents than lower level functionaries." I would argue further that high-level corruption creates a climate favorable to low-level corruption. If the head of the Department of Transportation is devoting considerable time to making sure that a new highway runs past land that he owns, that official probably will not be paying much attention to subordinates who are fixing parking tickets. It would be nice if we could count on effective political oversight to reduce high-level corruption, but often we cannot, especially in the context of developing countries.

I have argued elsewhere that the degree to which top positions are filled by promotion from within the bureaucracy can influence the level of venality of high-level officials, and thus the level of low-level corruption as well (Rauch 1995). My argument is as follows.

Many civil servants care about power as well as money. The head of the Department of Transportation may have a vision of what kind of transportation system his country should have, as well as a desire for personal gain. He will have a hard time implementing that vision if the department is full of no-show jobs and deputies are busy working out kickback schemes and the like. Such a department head will therefore spend more time supervising his subordinates to make sure they do their jobs and do not waste the department's funds, and he will have less time to create extra rents for his own consumption.

If I am correct, society is better off if department heads place a high value on the exercise of power in the sense of imposing their preferences about collective goods on the public. Assuming that one cannot rely on politicians to appoint such people, I believe that a system of promotion to department head from within the deputy ranks will increase the odds of such people becoming department heads. Those deputies motivated only by desire for wealth will want to enjoy the low-level corruption currently available to them and will want to be promoted and enjoy high-level corruption. But a power-hungry deputy will want promotion even more and can be expected to take more ac-

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tions to increase his chances. Those actions will include restraining his current low-level corruption. In a bureaucracy that promotes from within, deputies who care about exercising power are thus more likely to become department heads, and it follows that department heads in such a system are more likely to care about exercising power. This creates a virtuous circle, since such department heads spend more time supervising their deputies and are thus more likely to weed out corrupt ones, leaving only those who restrain their corruption available for promotion.

Work that Peter Evans and I are doing on the influence of bureaucratic structure on bureaucratic performance is in part motivated by this argument. We are collecting data from experts on various countries on bureaucratic structure as represented by the core economic agencies. Our questionnaires cover career paths, recruitment practices, and pay. The idea is to see whether variables representing bureaucratic structure can help explain performance, including the prevalence of corruption, as measured by the indices produced by various private country risk services, such as those used by Paolo Mauro (chapter 4). We control for other variables that might be expected to influence bureaucratic performance, in particular the income and average level of education of the country.

Our definitive analysis is not yet complete, but we have some preliminary results based on incomplete data for 25 of the 35 developing countries in our targeted sample. Of six performance measures, bureaucratic structure was found to have a statistically significant and positive influence on four. Career path variables, including not only internal promotion but also security of tenure, were the most influential for the corruption performance indicator derived from the International Country Risk Guide, whereas salary and meritocratic recruitment were the most influential variables for better performance on the Business and Environmental Risk Intelligence indicator of bureaucratic delay and the Business International red tape indicator.

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