

Presentation by Pieter Bottelier on Corruption, International Business and Development for a Seminar on Corruption and Bribery in Foreign Business Transactions: New Global and Canadian Standards, Vancouver, B.C. 4 - 5 February, 1999.

I applaud the initiative of the International Centre to focus on corruption and its impact on development. We take it almost for granted today that this subject can be discussed openly at national and international conferences. That was not always the case. The greater willingness to discuss corruption openly appears to be associated with a decline in official tolerance for corruption in many countries. This leads me to raise three questions:

1. Why has the official tolerance for corruption declined during the past decade, in so many countries and institutions around the world?
2. What have we learned about the relationship between corruption and development?
3. What have we learned about how to fight corruption?

It is indeed remarkable that in the space of a few years corruption has moved to a very explicit and prominent place on the agenda of practically all international development agencies, including the World Bank, and many national governments. Ten years ago, one could only talk about corruption in the World Bank in a soft voice. Many privately admitted that there was a possibility that at least some of the official aid money would end up in the wrong pockets, but the problem was thought to be beyond our capacity to solve or even measure. Audit reports confirmed that project documents and accounts were nearly always in order and that was all that mattered. The less one talked about the possibility of corruption, the better. There was, moreover, a rather widely held view that a little corruption was not necessarily bad for development if it helped to grease the wheels of a slow and inefficient administration.

Today, corruption is a frontline issue in the dialogue between the World Bank and many of its member countries. It is also the subject of a lot of empirical research, international conferences and technical assistance programs for member countries that wish to fight it or simply understand more about it. The "C" word is no longer taboo in the World Bank. On the contrary, it has become a popular subject for open discussion. One can become an expert on corruption, like the Bank has experts on malnutrition or irrigation. Methodologies are being developed for the measurement of corruption. What has brought about this see-saw change in so little time?

Several factors have been at work. With regard to corruption involving international business, which is the focus of this conference, globalization and the growth of Multinational Corporations (MNCs) have undoubtedly been major factors.

Globalization has promoted the growth of Multinational Corporations (MNCs) and vice versa. According to World Bank estimates, MNCs now account for over 40% of world trade, acting as buyers, sellers, or both. Indeed, the global market has become the arena for competition between MNCs.

Globalization inevitably leads to pressures for the convergence of economic policies and institutional arrangements between countries. These include pressures for the adoption of uniform accounting and auditing standards, comparable business disclosure standards, common principles for the supervision of financial systems, for contract law, bankruptcy law, etc. These pressures will only intensify in the next century. The resulting trend towards convergence of trade and finance related policies and institutions between nations participating in larger regional or global markets will also entail pressures for higher standard of accountability in business and in government. These factors have contributed to the observed reduction in official tolerance for corruption. Whether reduced official tolerance is also associated with reduced incidence, is a different matter which I shall not try to answer here.

In light of the dynamic globalization forces, it is not surprising that some of the pressures for greater transparency in economic and financial transactions have come from the international business community itself, particularly from MNCs. At the same time, many governments of developing countries have realized that it is in their own best economic interest to establish a more level playing field for enterprises and to eliminate corruption as much as possible. Pressures also came from donor governments and non-governmental organizations such as Transparency International. More recently, the World Bank added its voice to the chorus. President Wolfensohn's decision in 1996 to place corruption squarely on the agenda of the World Bank as a key development issue, was historic. It has contributed to changes in the way the Bank views development, and conducts its business.

Globalization is not good news for all. It has acquired a bad name in some developing countries in the wake of the financial crises that swept around the world in recent years. This has led to a reversal of globalization policies in some countries. I do believe, however, that such reversals are likely to be only temporary. The technological, economic and social forces driving globalization are so strong that it is hard to imagine that any country can permanently insulate itself from these trends without falling behind in development. The answer to the problems that premature or poorly managed globalization has brought to some developing countries does not lie in turning the clock back, but in establishing national and international conditions under which it is relatively safe and advantageous to participate in global markets. Some temporary restrictions on unwanted short term cross border capital flows are not inconsistent with globalization.

Whilst generally, globalization generates forces that tend to reduce official tolerance as well as the space for corruption, some aspects work in opposite direction. For example, money laundering becomes easier when the financial proceeds of crime, corruption and drug sales can be freely transferred from country to country in open international capital

markets. The globalization of financial markets facilitates cross border financial fraud. This puts a special responsibility on banks and other financial institutions to recognize the tell tales of money laundering in international transactions. Although progress has been made in this regard through staff training, electronic scanning of transactions and agreements among banks to exchange certain kinds of information upon request, the problems of international money laundering and other forms of financial fraud remain very serious.

If globalization tends to narrow the space for corruption involving international business, it is logical to expect that the same forces will project down to business transactions in national markets. In an interdependent world with open markets and instant electronic communications, where commerce and financial transactions are dominated by MNCs and international banks, it becomes increasingly meaningless to distinguish between national and international markets. Pressures for the harmonization of policies and standards will be felt at all levels in countries that wish to stay ahead in the quest for modernization and development. The logic of modernization with globalization is that official tolerance of and space for corruption will both continue to narrow.

Let me now turn to the second question: what have we learned about the relationship between corruption and development. The answer is a great deal. Empirical research by the World Bank and others has established that there is a strong negative correlation between corruption and development. This does not mean, however, that development automatically follows once all corrupt parties are identified and locked up, or that development automatically slows as soon as corruption becomes part of the picture. There are plenty of examples to show that economic growth and serious corruption can coexist for a period of time. But such growth is generally not sustainable in the long term. A culture of corruption breeds deep societal and often also serious environmental problems. It undermines democracy and the credibility of government. Corruption, like ignorance, is an enemy of sustainable and equitable development. There is also overwhelming empirical evidence that, over time, there is a strong positive correlation between good governance and development.

Systemic corruption is often associated with underlying political or societal problems. Once it has become part of a culture, it is extremely difficult to eradicate. Freedom House concluded on the basis of empirical research that there is a negative correlation between bribery and civil liberties and also between corruption and women's rights. Corruption is often associated with excessive and/or discretionary regulation. High taxes also tend to promote underground economic activities and other forms of tax evasion and corruption. Inadequate pay for civil servants, usually due to the weakness of fiscal systems, or unfair staff promotion policies, can have similar negative effects.

Political systems that tolerate or even promote unequal opportunity, unequal protection under the law, monopolistic practices, restrictions on information, racial discrimination, etc. are more prone to develop a culture of underground activity and corruption than

systems that pursue policies aimed at social fairness, equal opportunity, fair competition and open communications. Similarly, countries with a strong administrative capability and well established institutions are less prone to corruption than countries with weak administrative capability and weak institutions.

This brings me to the third and last question: what have we learned about how to fight corruption? Since corruption is often an expression of underlying societal or political problems, strong anti-corruption laws and prosecutorial capacity, though necessary, may not be enough. The experience in many countries shows that fighting corruption may require changes in social behavior and values, institutions, power relationships and political systems. But the single most important factor in fighting corruption is political will. If there is political will, the World Bank is prepared to assist member countries in a diagnostic review of the corruption problem. This may help to assess the extent of corruption and identify possible underlying social, cultural or political factors. If a country is unwilling or politically unable to fight corruption, it will also be unable to modernize and develop in a sustainable and equitable way. Most external development aid and technical assistance provided to such countries is likely to remain fruitless. Such aid could even have the perverse effect of making the problems of underdevelopment worse.

Assessing and combatting corruption in transition economies such as China and Russia presents special challenges. Transition to a more decentralized, market-oriented economic model is an extremely complex process implying, amongst many other things, that the role of the State in the economy has to change fundamentally. Such changes require a period of adjustment, the length of which can vary greatly. They involve deep societal, institutional and transactional change. In a large and diverse economy such as China with regions that are at very different levels of development, the State cannot create functioning markets and transform its own role in the economy very quickly, even if the leadership has the intellectual conviction and the political will to pursue such fundamental changes.

Having observed the Chinese scene close-up over an extended period, I have come to the conclusion that quick transition is physically, socially, economically, administratively and financially impossible in a large and diverse country where most people have become used to a totally different way of thinking about development and State-society relationships. In most situations, there is no realistic alternative to a gradual transition. But this presents enormous challenges of management and sequencing. There will be a period during which elements of the old and the new economic systems overlap in varying proportions as we see today in China and Vietnam. Opportunities for corruption may multiply until genuine market competition, a new legal system and institutions with adequate regulatory and supervisory capability are firmly established.

It is during this twilight zone of transition that foreign enterprises are often faced with serious dilemmas on how to conduct their business in and with the countries. Frustration over administrative delay or excessive regulatory discretion will be mixed with temptation, and sometimes ample opportunity, to corrupt underpaid officials on the other side of the

table. The pressure for corruption may also come from the other side. Sometimes, corruption creeps in primarily as a result of excessive regulation or a culture of discretionary decision making by public officials.

The special difficulties of economic transition provide an opportunity for leadership by MNCs and other large corporations with long term vision and interests. It is a time when strong codes of voluntary business ethics can be particularly critical. Such codes exist within many developed countries and their business associations. International business should not hide behind the institutional weaknesses of developing countries and transition economies. They should collectively and individually position themselves to contribute to the development of sound business practices and transparency in the countries in which they operate. Several large corporations have already adopted such voluntary standards of corporate behavior. It is in fact a form of development assistance which can be extremely powerful and effective. Perhaps more powerful and effective than anything multilateral development agencies can achieve through projects and technical assistance.

If I may express one, at this stage perhaps still utopian wish for the next century, it is that the international business community through trade with and investments in developing countries and transition economies contribute to the fullest possible extend to sound business practices and transparency wherever they operate. Banks and large international financial service companies such as the remaining 6 big sisters, are in a critical position to support this objective. Corruption may yield profits in the short run, but it undermines development in the long run. We should recognize the principles of transparency and accountability as economic fundamentals, just like sound monetary and fiscal policy. Conferences such as this one can help to remind us of our collective responsibility for long term and sustainable development in the global village.

Thank you.