

What has our grandchildren got to do with corruption? *

by Quah Boon Huat

The issue of corruption has always been in the news, but more so recently. It actually led to a somewhat heated debate with a colleague recently on whether public sector corruption contributes towards inflationary pressures. More on that later.

“Graft fuels Indonesia’s infrastructure woes: Analysts”, says a recent news report from AFP, the global news agency. The sudden collapse of Indonesia’s longest suspension bridge in November, which killed more than 20 people, had triggered the report.

Transparency International’s Corruption Perception Index ranks countries according to how corrupt their public service is perceived to be. According to Transparency International-Malaysia, Malaysia took 60th spot this year, a drop of four places from last year. It scored 4.3 on the survey, far behind Singapore (9.3) and Brunei (6.3). Malaysia is among 60% of the countries surveyed that scored below five, and its underperformance has certainly whipped up debates about the seriousness of public sector corruption in Malaysia.

In an immediate response to Transparency International-Malaysia’s announcement of the 2011 Corruption Perception Index, the government’s Performance Management and Delivery Unit (PEMANDU) announced that it is pursuing corruption-related issues very seriously. That’s because corruption can mean failure for both the Government Transformation Programme and the Economic Transformation Programme.

Below are some examples of how corruption can affect long-term economic growth and development:

1. Corruption has a negative impact on productivity, which is absolutely critical for sustainable long-term economic growth, because it raises the costs of doing business. The AFP news report on graft in Indonesia reported that a “World Bank analysis found corruption could add up to 20 percent to the existing costs of projects in Indonesia.”
2. Corruption deters investments because it is comparable to a tax on investments. For example, the AFP news report on Indonesia reported the London-based risk consultancy Business Monitor International as saying that “high levels of corruption have severely impeded investment in the country's infrastructure from non-public sources”.
3. Corruption causes inefficient resource allocation because decisions of public officials or politicians will be biased towards transactions that offer more opportunities to strike corrupt deals. Resources would thus be wasted on projects that have no economic basis.

Coming back to my debate with my colleague, does public sector corruption contribute towards inflationary pressures? What does economic theory say?

As corruption is a very broad, complex phenomenon, and not every type of corruption may have the same economic effect, it may be useful here to differentiate between the different types of corruption: a) grand corruption (which involves large sums of money, senior officials, and major decisions) and petty corruption (which involves small sums of money,

low-level officials, and the provision of routine goods and services); b) systemic corruption (which permeates an entire agency, ministry, or even government) and individual corruption (which is isolated and sporadic); and, c) syndicated corruption (in which there is an elaborate system to receive and disseminate bribes) and nonsyndicated corruption (in which individual officials seek bribes on an ad hoc and uncoordinated basis).

It is obvious from the above that the economic impacts of grand corruption, systemic corruption, and syndicated corruption can be significant because of their scale. One would expect them to have a larger economic impact, e.g. inflationary pressures, when compared to petty corruption, individual corruption or nonsyndicated corruption.

According to simple economic theory, corruption, which is a form of tax, decreases aggregate supply. That is, it shifts the economy's positively sloped aggregate supply curve to the left. Assuming that the economy's negatively sloped aggregate demand curve remains stationary, the aggregate supply curve's leftward shift implies a rise in the aggregate price level.

Mounting public sector expenses as a result of corrupt public sector officials siphoning off public funds meant for development can lead to the government printing money to finance the country's budget deficit. Economic theory says that such a move would raise aggregate demand, i.e. shift the economy's negatively sloped aggregate demand curve to the right. Assuming that the economy's positively sloped aggregate supply curve remains stationary, the aggregate demand curve's rightward shift implies a rise in the aggregate price level. Zimbabwe's recent episode of hyperinflation is a case in point. Some blame it on the government's printing at will worthless currency to try pay its way out of trouble.

Economic theory thus says that public sector corruption contributes towards inflationary pressures. The degree of contribution however will depend on the scale and extent of corruption that's taking place, e.g. whether corruption is institutionalised. Institutionalised corruption in Zimbabwe has been blamed for the country's recent inflation woes.

Corruption is insidious. It may seem harmless to those who do not come into direct contact with it. But we are all affected by corruption; for example, you "pay" for it in terms of higher prices when you shop at your favourite convenience store.

In the long term, your children and their children will continue to pay for corruption in terms higher prices; in addition, they will pay for it in terms of a lower standard of living.

The writer is research fellow at the Malaysian Institute of Economic Research (MIER). Opinions expressed here should not be attributed to MIER.