Foreword

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The global financial crisis has prompted a rethink about growth models in several parts of the global economy. Once the deepest phase of the recession is over and the immediate causes of fragility have been repaired, it will be impossible to go back to business as usual. Growth models will have to be reconsidered, priorities will have to be restated, behavior and incentives will have to change to make growth more sustainable, more balanced, and more equal. This will require a strong push for structural reforms, delivering better labor markets, more competition in product markets, more efficiency in public administration. Available evidence indicates that structural reforms can increase potential growth rates by significant amounts while helping achieve fiscal consolidation and minimize social exclusion.

Structural reforms deliver results if they are well designed, but, also, if implemented effectively. This is where corruption enters the stage as a key determinant of success or failure in structural adjustment. As this very comprehensive and fascinating book by Marco Arnone and Leonardo Borlini shows, corruption can undermine the economic process in several interconnected ways. When dealing with public officials, there is a risk of a conflict of interest which increases as more space is left to discretion and the opportunity for corruption increases. This is relevant in the area of public spending as well as in tax collection, where the incidence of bribery increases as the system gets more complex. Corruption also proliferates where governance is weak since weak governance in both the private and public sector increases the areas of discretion.

A finding which bears directly on the impact of corruption on growth is the evidence that, where public and private corruption proliferates, markets are dominated by distortions and inefficiencies; in turn, the malfunctioning of markets generates advantages only for privileged lobbies, who are the insiders of the corrupt structure.

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In addition to undermining competitiveness, corrupt markets do not attract international capital flows and are associated with low growth (due to additional barriers to entry and the higher risk to investment caused by corruption). In short, corrupt countries are at a disadvantage compared with others. And the book documents the negative relationship between corruption and income per capita that holds for countries worldwide, including advanced, emerging, and developing economies. Fighting corruption is also a key principle when thinking about public administration reforms. Indeed over-lengthy bureaucratic procedures are generally associated with high levels of corruption.

On the bright side, the book documents the fact that economic crises lead to greater social responsiveness in the face of attempts to conceal cases of corruption. At the same time, when the need for fiscal consolidation following a crisis is large, thus leading to a reduction in public expenditure, conflicts between companies for limited public resources are exacerbated. This generates tensions that eventually lead to collaboration with the investigating authorities or, at least, make it more difficult for agreements to be reached and sustained on what to keep hidden.

Another important element related to the financial crisis is that corruption can affect the performance of financial markets and instruments, be they sophisticated as in advanced economies or still in their infancy, as in developing countries. Also, corruption affects the financial performance of firms, be they large listed corporations or relatively small microfinance institutions. The main point is that global investors require a substantially greater return on debt when the issuer is a more corrupt country. Conversely, a well-functioning and transparent financial system is a strong antidote against corruption. Indeed corruption is negatively correlated with quality and transparency of supervision; hence, transparency-based reforms of supervision would be useful to achieve multiple objectives (better institutional governance, better supervision, and lower corruption).

The second part of the book looks extensively at the legal instruments available at national and international level to fight corruption. The reader will find this part just as fascinating and useful as the first one. I would like to mention one aspect in this respect. The absence of corruption is a public good. A corruption-free global system would be a global public good. As is well known, public good production requires strong collective action and effective international collaboration in multi-country environments. One lesson from the global financial crisis is that global governance has lagged behind market integration, making the global system more risky and the costs of the crisis larger. Building a more stable and equitable global economy requires, as mentioned, a strong effort in structural reforms and adjustment. A stronger global governance is something that requires a corruption-free environment while being, at the same time, a powerful instrument to fight corruption. This requires, among other things, strong international institutions.

International approaches to fighting corruption are already bearing fruit. For example governments that adhere to and actively enforce anti-corruption standards, such as those in the OECD Anti-Bribery Convention, send a strong message to potential foreign investors that they are committed to providing a clean and stable environment for business. But there is more to it than that. Governments that adhere to the enforcement of international standards usually encourage their companies to adopt appropriate internal controls, ethics and compliance measures. These companies can more easily enter the supply and distribution chains of larger companies that are increasingly doing due diligence when contracting with third parties to avoid liability under domestic anti-corruption legislation, such as the United States Foreign Corrupt Practices Act and the United Kingdom Bribery Act.

Let me conclude with some warm thoughts about Marco Arnone. Marco was a great economist and a very good friend. I had the privilege of sharing with him many reflections and some work in the areas which he privileged, that is the deep and complex interactions between economics and institutions. As this book demonstrates, he mastered these issues quite thoughtfully. I learned a lot from him. Thank you Marco.