



TRANSCRIPT OF DEVELOPMENT DRUMS [EPISODE 20 – CORRUPTION]

Host: Owen Barder. Guests: Mushtaq Khan & Daniel Kaufmann

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Owen Barder

This is Development Drums Number 20. My name is Owen Barder in Addis Ababa. Today we've got a really interesting discussion about corruption. And I'll be joined by my guests, Daniel Kaufmann and by Mushtaq Khan. Before I introduce my guests, let me say a big thank you to Alison Evans who took over this seat for Development Drums 19, and to the folks at ODI for making that episode possible.

I am joined by Prof. Mushtaq Khan, Professor of Economics at the School of Oriental and African Studies, or SOAS, here at the University of London. Mushtaq, thanks for coming on to Development Drums.

Mushtaq Khan

My pleasure.

Owen Barder

And I am also joined by Daniel Kaufmann who is a Senior Fellow in Global Economy and Development at the Brookings Institution. And he was previously the celebrated director of the World Bank Institute. And he led work there on governance and anti-corruption. His areas of expertise are public sector and regulatory reform, governance and anti-corruption. Daniel, thanks for coming on Development Drums.

Daniel Kaufmann

Thanks, Owen.

Owen Barder

Let's start with I think an issue that a lot of people who are not development experts find puzzling, which is why it is that common sense tells us that corruption is an important issue and yet a lot of people who work in development seem less concerned about it than perhaps popular opinion out there suggests they should be.

And really one way of phrasing this question is whether corruption causes poverty, which I think, Daniel, is something that you've argued quite strongly, or whether it's the poverty that causes the corruption, which is something, Mushtaq, that you've argued we should focus on.

Let's try and unpack. I mean, presumably, in some sense both is true. But let us try and unpack which way round this causation is working. And, Daniel, if we can start with you, you've claimed that countries can get a very large dividend from better governance. What's the evidence that you would want to point us to that if we could tackle corruption we'd get faster poverty reduction.

Daniel Kaufmann

Well, at one aggregate level, we can point to the work that by now a number of academics have done that we – we did it with Aart Kraay long time ago, almost a decade ago, which is a 300% dividend, development dividend of good governance and anti-corruption we call it. So a country that makes a serious effort and does improve in controlling corruption can expect in the very long term so that payoff takes place over a very long period of time, and expect a threefold increase in per capita income, going from 1,000 to \$3,000 per capita per year or from 4 to 12,000 and –

Owen Barder

And that's just from tackling corruption. Just by tackling corruption you can get from 1,000 to \$3,000 per capita income.



Daniel Kaufmann

Well, you are getting already into a complicated arena because one of the things that they have for better or worse quoted me many times is the expression that one doesn't fight corruption by fighting corruption. So there is no such thing as just tackling corruption; by just instituting an anti-corruption commission or adopting another law that won't work. One has to look at the quality of all the key institutions; whether there is a free press, democratic accountability, the issue of property rights. So you have to do homework on governance in general to tackle corruption. There is no such thing as just tackling corruption.

Owen Barder

We'll come in a second to the question of how we tackle corruption and what the best way of doing it is. But Mushtaq, what's your take? Do you buy this idea that if you can find a way to improve governance in corruption that that enhances growth and poverty reduction?

Mushtaq Khan

Look, there's absolutely no dispute that if you compare rich countries, which have achieved development and you look at their levels of corruption and you compare them with poor countries, which are struggling and are poverty-stricken and so on, there is a huge difference in corruption between them, okay? So rich countries are generally less corrupt and they are rich. And poor countries are more corrupt and they are poor. There is absolutely no question about that.

Now the question is, so if you – the problem is to show what are the preconditions for getting from poverty to prosperity. That's what the policy issue is really all about. Nobody is disputing that corruption is a bad thing, that corruption has a lot of negative effects, that corruption damages people, that we would all love to live in a corruption-free world. I think those are not issues at all. There is no disagreement amongst anybody on those things. And a country with lower corruption is better than a country with higher corruption, period.

Owen Barder

But specifically, to Danny's point which – his work with Kraay that if you can reduce corruption, then you reduce poverty. Do you believe that?

Mushtaq Khan

No. I think there the debate becomes extremely complicated. There are many different types of corruption, number one. Some types of corruption can be reduced in poor countries and will have a dividend on development. But there are many other problems in developing countries, and the question that you've posed at the very beginning is vital which is, why are all poor countries corrupt?

And the answer is not a simple one that poverty causes corruption because poor people are hungry, so they steal. It's not that simple because actually if you look at poor countries, the poorest people are not corrupt at all. It's not the poor who are corrupt. It's – somebody else is corrupt, okay? And so the question really is why are emerging ruling classes in poor countries so corrupt compared to ruling classes in rich countries?

And if you put that question in that historical way, a long-term historical question, I think econometrics can't answer those kinds of questions, so I have a real problem with econometric approaches for establishing causality there, and the question is a slightly different one. There are a number of structural features, which I have identified in my work, which means that – which shows that developing countries are structurally more corrupt and there is nothing much you can do about in the short run. And can I give you a couple of examples?

Owen Barder

Before you do, let me just check with Danny. So here the proposition is that poor countries are structurally more corrupt and so you need to tackle the poverty to tackle the corruption. Daniel, do you buy that?

Daniel Kaufmann

No. Look, I think at some point one has to move beyond – and I agree with Mushtaq – beyond the lofty econometric debate. We claim, and there is a set of about four or five refereed articles in the best journals



that one can untangle causality with the best econometrics from countries all over the world, and one shows that there's a causal link going from first improving governance and anti-corruption to better development outcomes including growth and incomes.

The reverse causality is debatable. Some like us have not found much play because there are countries that get a lot of money from oil and have not been able to transfer that into better governance and others have done well. So on average, it washes out. But that's a debate we can have until midnight. I agree with Mushtaq that it's not enough just to look at these big econometrics studies.

It's very important to go to the micro data. We have shown at the project level just using all the development projects that the bank has funded that where there is corruption, in general, in the country that affects essentially the delivery, the implementation, the quality and whether the project succeeds or fails. There is a lot of evidence at the country level.

There is this great book that everybody should read that just came out about Kenya, *It's Our Turn to Eat* by Michela Wrong. I think rather than having very lofty academic and econometric arguments, which we can do for three days, the more we look at what's happening on the ground. I have seen what's happening in Chile, my own country, and how it has made it by improving governance and anti-corruption compared with its neighbors or compared –

Owen Barder

Let's hear from Mushtaq on his answer to that point, which is in a sense it stands to reason that if you improve corruption that that reduces poverty but also the point you – that I interrupted you before you were about to make, about the ways that entrenched elites in poor countries, that there is corruption inherent in that system.

Mushtaq Khan

I think that the big methodological issues about evidence and data are actually vitally important, okay? If you compare countries with slightly more and slightly less corruption, and slightly less and slightly higher growth rates, it is true that – and I have no dispute with Danny, that everything else being the same, a little less corruption is better.

The question is – the problem that Danny doesn't look at is if you look at every successful transition, if you look at the China, the South Korea, the Malaysia, the Thailand, the Japan before that, okay, what was the process through which countries actually developed as opposed to comparing Kenya with Tanzania and so on.

There's no historical evidence of a country which first reduced corruption and then developed. This is my problem with the whole econometric exercise. And the reason for that is – the reason why you can't do that are those structural reasons, which we really need to understand.

So, one problem is that poor countries are going through transitions. They are going through huge social change. The problem of corruption is that if you have a stable ruling class, if you are a poor country but you are stable, then the ruling class is legitimate. You will actually have very low corruption.

The Mughal Empire was not very corrupt. India today is highly corrupt, why, because it's going through an enormous social transition. New classes are coming up. New forms of social organizations are coming up. In rich countries, there is a lot of mechanisms through which the rich preserve and protect their privilege and acquire privilege and in economics, this is called rent-seeking, okay?

The difference is that in rich countries a lot of the rent-seeking is legal. Some of it is very damaging. And some of it is not so damaging. And some of it is very beneficial but it's legal. The problem in poor countries is that much of that rent-seeking, the way through which emerging elites buy themselves privilege and protect their assets and so on is structurally illegal because they are not legitimate yet. It's a process of transition.



And that happened actually by the way in some relatively rich countries like Eastern Europe when they were going through their transitions you had very high spikes in corruption. That kind of corruption is produced by the process of transition itself.

We should get away from that legal versus illegal division between rent-seeking and go down to what I think is much more important, which is why are some types of rent-seeking so damaging and how do we address those, and why are some types of rent-seeking in transition economies actually structural, which we can't do anything about. And if we try and attack that actually we do damage the patient, it doesn't help the patient.

And there's one other type of corruption, which is absolutely fundamental in poor countries, which I think economists don't really understand, and that is political corruption. And the reason why all developing countries have significant amounts of political corruption 'til they're middle-middle income is that the way in which you buy political stability in rich countries, which is by having a 30 to 40 to 50% tax base and then redistributing a lot to people is just not possible in poor countries. So you can't achieve political stability through that mechanism.

There are huge aspirations. There are huge instabilities and violence and wars going on and civil wars going on. Elites in developing countries achieve stability through processes of patron-client politics where, to put it very crudely, what they do is they identify the most powerful and the most dangerous coalitions and they buy them off, and they include them in the government. And the fight is between different coalitions of very dangerous people.

That kind of political corruption is – if you try to tackle that you actually blow those countries up, okay? So you need to understand what you're doing. There are some very damaging types of corruption, which we need to address. And you don't identify what those damaging types are through regression exercises.

Owen Barder

Let's come on in just a second before – to the question of what kinds of governance improvements matter and matter for development and growth. But let me just go back, Danny, to give you a chance to come back on that point. Mushtaq's point is, if I may summarize it, and you tell me if I've got this wrong, that a part of the process of the economic change is to do with the redistribution of wealth and power and in an environment that is – essentially, we call that 'corruption' where it's illegal, and in poor countries it's inevitable. As they go through that process of change, there is illegal transferring of wealth and power. And that's part of the development. That's an inevitable part of the development process

Mushtaq Khan

And then illegal – illegitimate mechanism of protecting the assets of those who are themselves illegitimate because they haven't been there long enough. So it becomes legitimate.

Owen Barder

Daniel, there's no development without corruption?

Daniel Kaufmann

Look. It's not just no development, but there's no – nowadays, if there was any doubt that we know that there are no world affairs without some of the wheels being turned by corruption. The whole issue, there is absolutely no question, and let's just agree quickly on one issue of convergence and then let's discuss the most pressing issues of the day.

There is no question that at the end of the day, corruption has a huge element of being a symptom. It's a very negative symptom. The corruption is not the fundamental ill but causes everything else. Corruption in turn is related to political inequality, is related to all kinds of historical institutions and we can discuss very much which ones Mushtaq prefers, which ones I prefer. There is a whole literature from MIT, from Cambridge, from many places.



So obviously, corruption is a result also of many other problems. The issue of political inequality, the distinction between illegal and legal corruption, which we have written a lot about, is something worth noting and if anybody thought that poverty – still thought that poverty causes corruption, look at what happened in the financial crisis in the world.

Look at the Wall Street corruption which a lot of it was legal, was capture – one issue that we have not discussed yet which is part of political inequality is capture of the regulatory framework and of the state, but by particularly powerful financial and industrial firms and that happens in many, many countries. And I assume that Mushtaq would not disagree with those manifestations.

So which manifestation of corruption and which determinant of corruption matters a bit more or less, we can discuss that and there is a lot of areas of convergence and some of the areas of petty corruption may not matter as much as those grand corruption and some even legal corruption, which also happens in United States and the rich countries.

Having said that, I think we need to have a hard look at the data and be very careful in not putting in the same group, India and Kenya, for instance. In countries like Kenya, the type of corruption and the extent and the magnitude and what has happened including at the very, very top – it has a group.

And that's why I think we need to be much more practical, get into the country, understand the country, read these books like by Michela Wrong to understand the nefarious effect that throughout history, corruption and the associated misgovernance has caused as opposed to India which is in another league. There is corruption in India. There is corruption in Wall Street too but it's a completely different type and extent. And that's where we need to get into the country and look into that.

Botswana is a complete different story from very early on with anti-corruption and with better governance and Mauritius and Ghana and a number of other countries and have shown the way that by, from early on, fighting this and tackling these issues, they have managed to develop in a way that Kenya has stayed stuck for all these years, not to speak about Equatorial Guineas and other such countries.

So let's be very careful in not labeling India as totally corrupt as if it was a case like Equatorial Guinea because it's a complete misunderstanding of the evidence.

Owen Barder

Okay. So I think I am seeing some convergence here, Mushtaq.

Mushtaq Khan

I think this is remarkable. We are actually seeing some convergence with Danny Kaufmann. And I have been arguing for many years that there are many different types of corruption. And even within India, the corruption you find in places like Eastern Uttar Pradesh or Bihar is very different from the corruption you find in Tamil Nadu, which is very different from the corruption you find in Maharashtra. And I think this is precisely the kind of case study understanding of political-economic processes that we need to understand to be able to intervene effectively.

I think there is – having achieved that, let me actually push that convergence a little bit further.

Owen Barder

Don't rock the boat here; we've got a consensus.

Mushtaq Khan

No, no, no. No, no, I think there are some substantial differences.

Daniel Kaufmann

But you agree, Mushtaq, Mushtaq, if I can come in, but you agree that at the top in India, you cannot compare with the kleptocracies that we have known in other countries. At the top in terms of their civil service, in other words, and the top political leadership in India, is it as corrupt as some of the other



countries that you are putting in the same group? That would be a complete misunderstanding, as opposed to local corruption, which is also a huge issue in China, I agree, but one has to distinguish.

Mushtaq Khan

Yes, and my entire life's work, Danny, has been about distinguishing these things and saying that if you look at the aggregate amounts of corruption in some indicators – opinion surveys and so on, you actually don't understand the differences. And that's precisely what I had been saying. So the reason why India does better than Kenya and China does better than India is to some extent related to the nature of these political-economy differences and the types of corruption. That's exactly what I have been saying for a very long time. So we are converging.

Now the issue really is when you actually do your micro studies, there is one issue, which is, you shouldn't forget the big historical picture. If the kinds of issues which the Kenyan evidence points out which I think – here is another convergence, okay. I can agree with you completely that if you have an aid project or if you have massive theft in the delivery of public services then you are not going to develop, okay?

But there are lots of other things you need to actually achieve development. If you compare Kenya with China, with Malaysia, with even the bits of India, which are working relatively well, with South Korea and so on, is the difference between them primarily in the theft, which is taking place in projects, which undoubtedly is a difference or are there much more fundamental differences in the political organization of the transition and the way in which the transformations are happening in which new classes are coming up, in which new technologies are being adopted and so on, which I think are much more important so that if we focus our attention on getting a little bit of improvement in the corruption, which happens in projects, are we really going to see a transformation of Kenya into a China or even into a Malaysia or even into a Thailand. I don't think so.

So I think that while I agree with you that there are important differences in some aspects of corruption, there are other much more important political-economy differences which we forget, which we can only identify when we look at the historical process of transition that I am particularly interested in. And that doesn't mean that there are any simple answers.

And where the convergence is, is that we need to understand countries much better. We need to understand these processes of transformation much better. But we also need to keep our eye on the big historical picture. The big historical picture is a reason why China is developing and parts of India are developing and Korea developed before that is not just that their leaders were slightly less kleptocratic. How you measure kleptocracy is itself very important.

Chinese leaders or South Korean leaders in absolute amounts made more money than any African leader can ever imagine. The thing is that they made their money by actually developing their economies. So there the much more fundamental question is why do some elites make their money by destroying their economies and others make their money by growing their economies.

If you look at it in percentage terms, the percentage that the Chinese take might be less than the percentage that Kenyans take, but they make massively more, and they're massively richer. So, ruling classes in these countries are rich because they are sharing in the growth of these countries. We shouldn't forget that. So we have to understand deeper economic questions.

Owen Barder

Danny, what do you say to the argument that it isn't the differences in corruption that determine the difference to why these countries are developing? There are other bigger, deeper issues that determine why Kenya is on one trajectory and India is on another.

Daniel Kaufmann

Right, the difference is, it's a very important first cut. And there's no question that the overall difference and magnitudes in Kenya versus the magnitudes in India is a first cut big explainer [sic] but I agree that's



not enough. Then one has to look at the different manifestations. But then again, we have to be very careful with inference and with the data.

I have no evidence of how rich the top leaders of China got. They were not kleptocrats in my book and in the evidence I have. I would like to see the evidence that Mushtaq has to the contrary that those Chinese leaders – the issue is more at the local level and some at different party level and at the enterprise level, the state enterprise.

So I think we need to be very careful with that, like the statement made before about India. But –

Owen Barder

Let's put this to Mushtaq because I rather sympathize with that. I mean when you think of Mobutu flying in jumbo jets of flowers from Paris and things like that. Well, I don't see any Chinese leaders ever having behaved like that.

Mushtaq Khan

You are absolutely wrong. I mean if you actually look at the absolute level of Mobutu's pathetic little houses in France and his pathetic palace in his country and you compare that – I mean I've personally known Chinese bureaucrats in South Asia who are doing deals for public sector Chinese companies.

And if you look at their lifestyle, the clothes they wear, the cars they drive, the assets they control, it has a fantastically different magnitude and they are engaged in very close connections with their governments, with the governments in the developing countries interested to do business, they are public-private entrepreneurs. They combine political power with business. And they are superbly rich.

Now if Danny wants a figure, obviously you can't do a survey and say this is the asset base of –

Owen Barder

How much have you stolen?

Mushtaq Khan

But I think that in terms of qualitative observations of Chinese bureaucrats and Chinese public officials in business, forget in China because you can't go and look at them in China, but if you look at them in India, in Bangladesh and Africa and you compare them with the African counterparts, they are on different planets.

Daniel Kaufmann

Well, I think we need to make a very clear distinction between bureaucrats and the top political elite and the top leaders. I thought we were talking about the top leaders and, when we talk about kleptocracy, that clearly refers to the top leaders of their country.

And Mobutu, in terms of percentage of the country in terms of the way he stole the assets of the country, it's an extreme case but it's not alone. Marcos commanded more wealth in that sense. But I have absolutely no evidence that the top Chinese political leaders did that.

But let's move on. I think another very important statement that Mushtaq made and I think it's very important for policy today is historical determinants and understanding the history is absolutely crucial but perhaps because we come from a different background, from where we come, I have seen it in my own country, in Chile, yes, we can.

The importance of current factors, if you have proper leadership, which we have not discussed, who understand the importance of taking the bull by their horns and saying we want to join the 21st century, have good institutions, good governance, anti-corruption, this has been the effort in Chile well before we started growing at such a pace.



And we are not alone. There are the Baltics. There are the Botswanas. There are a number of cases throughout the world that show that you do not have to be rich to afford the luxury of good governance and have very good rating in terms of not being corrupt relatively speaking. Chile today rates better than many rich OECD countries, including the Italys, the Greeces and a number of other countries in the world. So we need to concentrate and look at those cases and the importance that leadership can make.

Owen Barder

You're listening to Development Drums with me, Owen Barder, in Addis Ababa and my guests, Daniel Kaufmann and Mushtaq Khan. If you have comments on this or any other episode of Development Drums, or if you would like to suggest topics or guests for future episodes, please do so by coming to the developmentdrums.org website or join the Development Drums group on Facebook.

Can we focus on this question of changes that we can make and, in particular, this question of what kinds of improvements in governance improves growth? Because I know, Mushtaq, you've written about the difference between governance improvements that improve markets and governance improvements that improve economic growth. And I – sometimes in this literature these things are all bundled up together as if this is all one and the same thing. Unpack for us what you mean by that distinction and why it's important.

Mushtaq Khan

Let me unpack it by connecting it with the discussion before. Danny said that he doesn't know of any evidence of kleptocracy in successful countries in the type that you see in Africa. I think the problem is that when you look at processes of accumulation in successful countries, they look different exposed, okay.

There is a lot of case study evidence now of what happened in South Korea in the 1960s under the early Park Chung-hee and his successors, what is happening in the provincial level in China, what happened in Indonesia, what happened in Thailand during the 1980s, which shows that actually the difference between the accumulation of political leaders in high growth countries and low growth countries is not that one takes a lesser amount. It ends up as a lesser percentage because what is happening in the successful countries is that the leadership is constructing growth. And if you share in growth, it always looks less kleptocratic than if you are trying to share or extract from stagnation.

So the political-economy question is what kinds of political leaderships do you need to have to construct growth and transformation? And this is what I call governance for growth. And what we need to learn (and I will come back to Chile and the Latin American examples later on) that the problem in poor countries making the transition is, putting it very bluntly, how do you construct humane and dynamic versions of capitalism. And this is a very difficult task because capitalism by its nature is not just, is not fair, and it's an ugly beast, right.

So when we're talking about markets, you actually miss the elephant in the room, which is markets have existed in developing countries for thousands of years. We don't need anyone to come and tell us about markets. India had markets when Europeans didn't know what a bath was.

The point is that to construct capitalism is something completely new. It's a different hierarchy in societies, different asset structure, it's very difficult to construct. You need to have a lot of elite cohesion to achieve that transformation without civil war breaking out. The problem with a lot of African countries and large parts of India as well is that that elite cohesion is very difficult to construct. The elites when they have cohesion don't have a long enough time horizon so that they do a lot of looting instead of construction of capitalism from which they will actually end up better off. This is the problem.

The issue with Chile, you see, is that in Chile the capitalist transition has already happened. It's not – as I said earlier, it's not a question of rich and poor. It's a question of transition. You can be a relatively middle income capitalist country where the capitalist structure is already there and you just then keep your 5% growth going. The problem with – you can be a much richer country, which is, let's say, state planned and you make a transition and then corruption and all these problems of elite cohesion break down. In Chile, that elite cohesion problem was solved through a lot of nasty historical processes which we all know about. So we don't need to go into the history of Chile.



But right now, Chile has got a cohesive capitalist structure, which is not going through any fundamental transformations. And so even as a middle income country, it can do some, what I would call, market enhancing good governance. This is not the problem in China or India or Thailand and certainly not in Kenya where the elite cohesion itself doesn't exist, the capitalist economy doesn't exist, rich or poor, and capitalist sectors are very small and subject to a lot of redistributed conflicts with different factions and political movements, which each are trying to enter the capitalist game. That's a very different political economy.

Owen Barder

So, Danny, what do you make of this idea that we need to think about governance reforms that promote growth rather than governance reforms that just promote markets?

Daniel Kaufmann

I mean 10 years ago, we could have had that debate. Today, and I have written about it, it's the era of the end of ideology and even if you look at the G20 and how there is no difference in major ideological terms including between the Chinas and the U.S. in terms of the fundamentals.

And the Obama administration understands that these major interventions that are needed in certain parts of the markets. So I would like to re-integrate these old notions, the distinction between growth enhancing or market enhancing by suggesting that the operative concept should be market-friendly approaches to ensure that there is sustained growth.

Now to ensure market-friendly approaches that are consistent with long-term sustained growth, governance is crucial. And we can get into all kinds of abstract social engineering of how to have a perfect construct for a country to do a transition but this is not a social engineering experiment at the academic level. This happens organically; each country with its own civil society, government nooks and crannies, have to go through. And let me suggest that we are grappling with major issues still in Chile today even though relatively speaking we are doing well exactly because of the still legacy of the Pinochet era where a few potentates still wielded enormous power in terms of subtle or not so subtle capture in the economy like in Wall Street. So this is by no means over.

So we can talk about transition in any country now this including what's happening now in the U.S. That's not very useful operative concept at a very practical level. At a very practical level, let me put it very much in front of you because there, I think, we agree with Mushtaq is not that one needs to fight corruption by fighting corruption. There are certain actions that need to be taken for more integrity and lack of corruption in aid and in projects and investment of course but how can we – who would disagree about the importance of transparency of a free press, of democratic accountability, of some contestability at the both political and economic level in terms of procurement putting everything on line. So let's discuss concretely because this is what the people in Kenya, the citizens in Tanzania, in China and so on because by the way these kleptocrats were not confined to Africa. Remember the Marcos – the Marcoses and there are others, not to speak of others that remain in other parts of the world including my own continent.

So let's discuss concretely. Does anybody among us three disagree that we need to focus on those fundamental? In the past 15 years I've been monitoring the data. There are many more countries with democratic elections but there has not been an improvement around the world on a free press; to the contrary, there are reversals going against that in terms of further, further censorship. The same in terms of civil liberties and so on. The same in terms of transparency, does not seem to be increasing apace, in terms of disclosure of assets of the politician. Why don't we talk about that rather than obstruct experiments in social engineering which is not how development takes place on the ground.

Owen Barder

Mushtaq, that seems a very fair challenge, because most ordinary people, not the experts in this topic listening to this podcast would be saying, 'hear hear' to that, free press, property rights, rule of law, democratic elections, what's wrong with that as an agenda? Why aren't those important things to pursue as part of the development debate?



Mushtaq Khan

You've opened up a whole new can of worms now, because exactly what you could say about corruption, you could say about meaningful democracy, accountability, transparency, and so on. Are these things achieved through a process of development and the deepening of a productive sector and a deepening of the middle classes and civil society or are there preconditions of development? And I could say exactly the same thing about that agenda as before and I think while there is conversions, there is also, and thankfully, also areas of disagreements, so we can keep talking to Danny.

I don't think just because every country is going through some process of transition that every country is in transition. The transition that a Kenya has to go through to even to get to a position where it can employ its people is very different from the transition that the U.S. has to get through to solve massively damaging rent seeking in its financial sector. I think the difference is in the kinds of transition. So market friendly won't – market friendly is a much older term than market enhancing and growth enhancing governance and so let's come down to the concretes. I think the concrete is, is it the case that if you have transparency you can solve problems. Our people in Kenya or in India or in any country you can – Bangladesh which is where I come from, are they not aware of who is corrupt? And how they are corrupt? Everyone knows.

The taxi driver you take from the airport to your hotel will tell you exactly who is corrupt and how they are corrupt and how much money they've made and they might even exaggerate a bit of what's happening. That doesn't help anyone to fight anything. Okay? Because the problem is the structural issues that we come down to. The same people who are complaining about corruption will vote for the most corrupt politicians because those are the politicians with the resources to protect them. Now these are the structural problems. If I am a voter and the only person who can protect me is a corrupt mafia boss and the honest guy can't collect any tax to deliver anything to me, what does it mean to say I want an open democracy and I want a free press?

The kinds of concrete issues that I would focus on are the concrete market failures that are constraining development. How do you actually construct a capitalist sector? How do you get land and resources to industry? How do you actually get the financing to industry in very risky areas where the market failures are so huge that the private sector won't invest and it would take a generation to solve it by doing the market enhancing governance of contracts and rule of law? The reason why China succeeds is that there are very ad-hoc pragmatic solutions to these problems at the local level, that's what Kenya should be learning about. China is not succeeding because it has a free press and an open democracy and all the rest of it, although that's very desirable, I have no problem with saying, 'yes, let's go for that, we want – I want that anyway'. But I don't think that the problem with – in Bangladesh is that people don't know who is corrupt, that the problem in Bangladesh is that people don't have political choices and there is no democracy.

We have lots of choice between different corrupt people to vote for and you elect one load of corrupt people or another load of corrupt people and everybody knows that they are corrupt, this is not the problem. The problem is: how do you actually construct the prosperity which will allow us slowly to construct a social democratic form of capitalism where through the distribution of fiscal resources you can actually achieve poverty reduction and a good life for the maximum number of people, that's my problem.

Owen Barder

Danny – so transparency is no use if you don't have a way to change the...

Mushtaq Khan

It's useful, it's better than not having it but it won't solve your problem.

Owen Barder

Danny?

Daniel Kaufmann

First, no one single action will solve the problem, this is unfortunately the very complicated social sciences, development and not physics, so it has to be a combination and there we all agree that it is context specific,



so there is no one template that one arrives to, either Bangladesh or Chile and this is a Bible. Which one are – which are going to be the priorities and it's very important to prioritize, are going to vary from one setting to another, each country's transition is different but there is going to be a set of four or five priorities to just name a number that one has to put effort on those and the complementarity. When I speak about transparency or reforms, that's an agenda that has to be complemented of course by enforcement, by institutional strengthening in other areas and so on.

But I am not talking about making corruption more transparent which has been made much more transparent through many other ways, I am talking about the fundamental institutional level in terms of electoral finance, campaign finance, much more transparency in terms of the assets of candidates, of politicians in terms of procurement, I can give you – we can discuss a very concrete list of about 12 things that the reformists in reformist countries are doing. Mexico is one of the countries leading that effort. But of course it won't suffice, but I mean that's obvious, the question is, which transparency or reforms and it's not just to say a number about corruption on who is corrupt again in the press. But which ones are crucial for which country and so on.

Now I would also throw to the group; we're in 2010 almost. 2010, every country has a market economy, with the possible exception of a handful which we could agree with, but Kenyans, anybody who has worked in this country; they all have it. The question is whether they are surviving, thriving, or operating in conjunction and with a helping hand of government or in spite of government. But there's no such thing as country that have not undergone a transition. In fact, I lived Ukraine in the transition from the Soviet to the post-Soviet era, there was even a market during the Soviet era which was mostly informal and underground and the transition took place almost immediately even in the worst governed transitions in the post-Soviet Union, they all have a market.

So let's get real and see then ask the question, what in a very practical way are the most important priorities that in every country would matter? And there is no one Bible, I agree with that. But again we have not focused sufficiently on leadership and how a courageous leadership and reformist can change the name of the game in spite of the importance of historical determinant because that leads to a lot of fatalism. Some of the writings would say it's all historically determined, and so much determinism when we have in Latin America, we and the neighbors have the same history, the same – the same – almost in every count on history and we have gone totally different ways, or Ukraine versus Poland, or the two Koreas, just taking case that is of two neighboring countries with very similar historical culture, geographical, colonial heritages. And they have gone very different direction depending on leadership, on reform, on governance reforms and so on.

Owen Barder

Can I ask about the role of outsiders in this, because one of the challenges for policy makers in development is what if anything external actors, whether it's aid donors or other governments or indeed civil society and others from abroad could or should be doing to promote various kinds of basic governance in developing countries. You talked, Danny, about the importance of leadership which makes me wonder whether that's just a historical accident. Let me start with Mushtaq, ask what do you think is the right role if any for external actors to promote the kinds of governance reforms you would like to see and the kind of broader governance agenda?

Mushtaq Khan

I think the external actors generally do a lot of damage because they bring in ideas which are half-baked and not very clearly defined, and some of it is evident in the discussion we've been having, right? I mean even two extremely well-read people like Danny and myself who have gone through the literature can't even agree about our terminology because it seems that Danny keeps criticizing me for saying things which I'm not saying and gets it tangentially wrong. I am actually saying that...

Owen Barder

I'm sure he'd say the same about you.

Mushtaq Khan



Absolutely. I'm actually saying that markets have existed for thousands of years; that's not the problem. The transition I'm talking about is not the transition to a market economy; that was a problem in Eastern Europe. The transition I'm talking about is a transition to capitalism. It's a particular way of organizing production in societies with a particular distribution of assets which creates incentives for technology absorption and technology use, which creates incentives for exporting and growth and production, and that is extremely difficult to construct, it's a very politically difficult and painful process of constructing capitalism.

And the issues of governance that I would focus on is to look at the social and political and institutional constraints which are blocking that which are vast and huge in developing countries and which are only tangentially and very indirectly connected to things like transparency and electrical processes and so on, which are all important, but it doesn't help me in asking why is it that Bangladesh only produces garments and can't produce something else which is equally simple and trivial? And I could go into very concrete market failures in institutions and financing, in land acquisition, which are to me the most fundamental things you need to solve in those context and transparency and other things that we are discussing don't address those growth enhancing governance issues. So the growth enhancing governance issue is I think very important and we don't have time to go into that.

Now in terms of what outsiders do, I think outsiders do a lot of damage by setting countries goals of governance which are actually unachievable. So what you come, I mean – and Danny has converged to some extent, but you know, 10 years ago a lot of people were saying, set countries targets for corruption, set countries targets for X, Y and Z governance indicators. If you bring down your governance indicator by two points you will have so many X percentage points of growth and so on. People were writing professional articles in refereed journals, in reputable journals of that time.

Now what happens is when you go to a country and you set that kind of agenda, you mobilize a lot of people and real people hate corruption in developing countries, right? So it's very easy to construct massive social movements fighting corruption, okay, because people don't like corruption, I don't like corruption, it's horrible. So you mobilize all these people, you focus the political effort in fighting something and then you don't actually explain to them that the problem is structural, that actually you can remove this government, put in another government.

In Indonesia they got rid of this horrible guy called Suharto, and they ended up with a very pious and good and profound leadership of Abdurrahman Wahid who really wanted to fight corruption, and he ended up in one year's time as corrupt as the previous one because his party, his structures, the way in which politics is maintained is corrupt. Now what you then end up with is something devastating, which is demoralization. You demoralize people because they begin to lose confidence in their own politics, in their own ability to change their lives, because you haven't constructed achievable goals of governance which deliver anything. And this is the real problem with outside ideas coming in, which, in a most well-meaning way, are setting agendas which cannot be delivered, and you have seen that again and again and again in many, many developing countries.

Owen Barder

Danny, we are setting targets that can't be delivered with the effect of demoralization?

Daniel Kaufmann

Well, the problem is in the notion of 'we'. I mean, first, all this data, and we have been very bold as you know on indicators and doing surveys. This data is an empowering tool for the reformists and for the civil society within the countries, it's not for an outsider to set the target. I mean, who would think that, although some organizations like to do that but obviously that's not very useful, that's for them to do and in fact looking carefully at the data is so important again to monitor what has been happening. In Indonesia over the past decade there has been an improvement in corruption from an extremely low base obviously but it's going in the right direction and that's moralizing for many people including the Minister of Finance who told me so that they like to look at these benchmarks and these numbers not because some outsider will tell them where they should be because they the reformist want to continue arguing for continuing that route.



The same with a – the reformist during the Yeltsin era in Russia and so on they used this, so these are empowering tools, so...

Owen Barder

So that's the limit of external interference is that we provide benchmarks.

Daniel Kaufmann

Let me answer that. So, one area is just knowledge sharing and data with all the problems and we should make it very clear with margins on error and so on but let's empower everybody who is asking for, and there is so much demand for that, these tools for them then to monitor to do a data-driven policy making and monitoring and to empower them for more reforms.

Second is to share the experiences of other parts of the world of other countries and some outsider is invited because they know and I have been in many countries when I accept an assignment is not to tell them what they should do is because they want to understand how others did it. These countries, the reformist countries nowadays they want performance-based management, performance-based improvement in governance, and they want to learn from the best examples from other places in the world and the outsiders can play a useful role in sharing information.

Finally aid in a much more selective and careful fashion that is – than sometimes too indiscriminately can be very useful not in pushing or conditioning reforms from the outside but once you have a committed leadership, with integrity, to support them because sometimes they need resources and particularly in poor countries which they cannot get from foreign direct investment in the first phase. So aid can be useful in complementing those reforms but they have to start from within.

Mushtaq Khan

See a lot of things that Danny says are very reasonable and at one level I don't disagree with him. Of course, knowledge, information and experiences it's all very important. The problem is that the way in which Western intellectual consensus is constructed. We are providing a very partial understanding of history and this is really a significant problem because I think that – I mean I worry that if you look at the historical examples of the really successful transitions in the last 50 to 100 years, if you look at the South Koreans, the Taiwans, the Singapores, the Malaysias, the Thailands, the Chinas, the one thing which is strikingly common to all of them is that outside advice played a very small role in their transitions. Right?

I mean the South Koreans did not listen to what the World Bank was saying; the Taiwanese didn't listen to governance advice, nor did the Chinese, nor did the Thais, nor did the Indonesians, and I – of course this is – I'm being rhetorical and slightly exaggerating this, I think that what each country has to find is its own political cohesiveness to carry out very painful and ugly transitions and I keep coming back to this. What we are talking about is a very difficult and painful transition where you are constructing a new society which is capitalist in a broad sense but which has many differences between countries, where the state plays a very significant role in the early setting up of industries, in technology acquisition, in the processes of transferring and transiting, from one economic structure to the other; those are processes which don't fit and sit very easily in the intellectual structures and liberal economics and good governance, political philosophies, which Western countries have.

And I admire and appreciate those values; I want to live by them, but I think that in many respects it's very difficult to live by them and actually carry out a transition in the humane, just and efficient way in developing countries, and this is the problem that actually it might be that if the Chinese were in Africa, Africa might have an easier time paradoxically than with all the advice and which creates aspirations, which creates ambitions but which are very difficult to satisfy and you actually end up with greater social discord and greater social dissatisfaction.

So at one level I agree with Danny. We need to have more information. We need to actually provide more examples and more history to developing countries but that should be on a more balanced way. I mean Chile is a very exceptional country to really focus on. We really need to look at China. We need to look at South Korea. We need to look at Japan. We need to look at Malaysia. Are those historical examples



understood enough in Africa? Are – do people really understand how South Korea, how Taiwan, how China, how Malaysia and what kinds of governance did they have to make those transitions.

Owen Barder

It strikes me that you are both being quite modest about what you think the role of outsiders should be. Even you, Danny, are talking about information benchmarking, lesson learning. I would think that most people who pay taxes to aid agencies think that we ought to be rather more sharp-edged than that; that we should be being tougher about not giving aid to countries, creating strong incentives for...

Daniel Kaufmann

Yes. Absolutely.

Owen Barder

Countries to tackle corruption.

Daniel Kaufmann

Absolutely.

Owen Barder

I'm just interested to know, Danny, do you think that's the...

Daniel Kaufmann

Absolutely, maybe I said it very quickly but I said it, aid and finance, and financing development plays an important role but I said very clearly we need to be more selective. And we need to be more selective in ensuring that it's good money that goes after basically good money go to – and a commitment to improve an institution's governance and anti-corruption rather than not being sufficiently selective or not selective at all where at the end of the day those that are making very serious efforts are denied very important resources which are important for the reform. So in that sense the complementarity between aid and advice is very important.

But also I agree with you, Owen, we should be – while we should not be very prescriptive in saying this is what's going to work in your country, that has to be organically generated from within the country and led by the country. We should not be shy about saying how it happened elsewhere but also about what doesn't work, and there is still a lot of mythology in terms of try this and try that, try, Singapore has been so successful, well, try Singapore in Kenya, good luck!

So in 2010 we need to be much sharper edged and much more realistic on the ground of what can work. So we are back to the very basic question and, Owen, you summarized this very well, is how we should not be diverted with all kinds of abstract constructs from the basic issues in so many countries of rule of law and, yes, it will vary according to their diagnostic what aspect of the judiciary is most important, rule of law is missing and what part of enforcement. The basic issue of transparency and disclosure and which five reforms are crucial are very important, of the free press, of democratic accountability even in the own way of the country doesn't have to be an Anglo-Saxon – totally Anglo-Saxon section approach but more democratic accountability and contestability in terms of their polity, it has to be part of this debate.

And I would like to hear from Mushtaq an alternative for that for any country that you would tell, no, go the authoritarian route or some other variant, thereof of managed democracy which seems to be a fad nowadays in the Russias, and in a lot of African and Latin American countries. How can we basically get away with these all kinds of extraneous arguments from the very basic issues which you yourselves set up Owen?

We need to go back to the basics because so many countries are getting away from that, and one excuse for that is the crisis by the way, where we are going to see, and that's my last point for now, we're going to see an increasing gap in governance institution and development outcomes because there's one group of countries which are essentially reformist and another group which are basically sitting on the fence and using it as an excuse for coming up with all kinds of anti-market or anti-capitalist rhetoric and for now we



cannot act unless we are giving a lot of money in any case nor reforms. So you're going to see some countries which are seizing this as an opportunity for reform after the debacle while others are going to stay further behind. So it's very urgent to get to these practical issues now and not too lofty and abstract of an argument.

Mushtaq Khan

I think it's extremely important not be lofty but I think the loftiness of Daniel's position is that he says that we should not be asking Kenya to become like Singapore which I completely and absolutely agree with. It would be ludicrous if I or anybody else suggested that Kenya should be like Singapore. My problem is that we are asking Kenya to be like Sweden and Norway, or like the United States, and that's the problem.

So the issue is not that we are setting Kenya a set of goals which are about how Kenya makes the transition to capitalism within Kenya in a way which is consistent with Kenya's internal politics and its history and its existing technologies. We are not sitting down and identifying the market failures in its land markets, in its technology markets, in its financial markets and fixing those; we are focusing on issues like transparency, accountability, rule of law and so on, which don't come from Singapore but they come from Norway, Sweden and the United States. And those are actually not achievable in any meaningful sense.

And I disagree with Danny that these are settings realistic and pragmatic reform targets. They might be in some detail in some specific areas but in general they are actually in country after country that I work in and I have knowledge of actually creating discord and social dissatisfaction because it's a reform agenda which is unimplementable.

And in terms of aid I think it's absolutely important there is a fiduciary responsibility to tax payers in rich countries that aid doesn't get stolen. There is absolutely no question about that. Aid has to be managed and we have to ensure that aid is not stolen otherwise taxpayers in rich countries will stop giving aid. There is absolutely no problem with that. The problem is setting countries reform and governance targets, which, from my perspective, should be focused on only one thing, which is we have to understand that what is happening here is not about making markets work or having more accountability or something abstract and lofty like that, it's something very nitty-gritty, which is, how do we move from our existing industrial and agricultural structure one or two steps up the value chain? What do we need to solve to do that? What are the market failures and institutional failures?

And those are the governance areas, those particular agencies which deal with land allocation, the particular agencies that are managing finance and credit to upgrading technologies, that's where if we spent a lot of our time and focus and got rid of the damaging kinds of rent seeking and corruption in those agencies and we understood that some rent seeking and some corruption might happen anywhere because it's very difficult to get rid of all of that if we had a very pragmatic and practical approach to that and built up institutions and agencies at a very micro level which address these specific issues of transition building capitalism, we would be making progress in Kenya without getting lofty and without getting unnecessarily profound.

Daniel Kaufmann

I'll just say one thing, United States, by the way, has to undergo a major transition, anybody who would suggest that anybody should follow the example of United States after what has happened and it's just a question of not only reading the speeches of Obama but also seeing some of the actions and wait – and just wait after the health reform packet is passed what's going to happen in terms of the renewed effort on the regulation of Wall Street and so on.

So there is absolutely no question that the United States has to go also through a transition and that's extremely important to understand on many of these countries rather than trying to attain the perfection of any U.S. model, I don't know who would say something like this, so these has to be put in perspective and it's not the issue of the Nordics either. But again we're back to the question of how in a very concrete way one can suggest when one goes to these countries good examples of good transitions in terms of their rule of law issues, in terms of their transparency issues, in terms of how to improve and make procurement



better, in terms of the competitiveness in their polity and so on and making a market, let markets function with the needed regulations. So that's the end of ideology.

Owen Barder

On what was very nearly a point of convergence that transition applies to countries both in the developing world and in the industrialized world. I'd like to thank both of you, Danny Kaufmann; thanks very much for coming on Development Drums.

Daniel Kaufmann

Thank you.

Owen Barder

And Mushtaq Khan, thank you for coming on Development Drums.

Mushtaq Khan

Thank you. And the meaning of transition is where we disagree. Thank you.

Owen Barder

Thank you both.
