Profiles of Corruption in the Middle East

Robert Looney*

Middle East leaders should ask themselves if they will be remembered for resting reform or for leading it.—President Bush[1]

Sadly, one would be hard-pressed to name a single Arab country in which grand corruption among high officials of the state was not endemic.—Paul Salem[2]

Introduction

Headlines reading: "Corruption Means the Poor Stay Poor in Oil-Rich State"[3] or "Millionaire Mullahs"[4] have become all too common. In fact, one is often hard pressed to pick up a reputable newspaper without some sort of corruption story on the politics, business or even in the sports pages. In countries developed and developing, large or small, market-oriented or otherwise, governments have been scarred by corruption scandals. In some cases, not only have prominent politicians lost their official positions, but entire governments have collapsed or been replaced.[5]

Historically, the United States government's concern with corruption in

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[1]Quoted in "Bush: West Erred in Tolerating Mideast Corruption," *CNN*, November 7, 2003, <http://www.cnn.com/2003/ALLPOLITICS/11/07/bush.mideast.ap/>.

[2]Paul Salem, "The Impact of Corruption on Human Develop in the Arab World: A Concept Paper," (New York: United Nations Development Program, April 2003).

[3]Michael Peel, "Corruption Means the Poor Stay Poor in Oil-Rich State," *Financial Times*, August 31, 2004, p. 16.

[4]Paul Klebnikov, "Millionaire Mullahs," *Forbes*, 172:2, July 21, 2003, p. 56.

[5]Michael Johnson, "Public Officials, Private Interests, and Sustainable Democracy: When Politics and Corruption Meet," in Kimberly Ann Elliott, ed., *Corruption and the Global Economy* (Washington: Institute for International Economics), pp. 61-82.

foreign countries stemmed from the belief that American exporters lost out on foreign deals because U.S. law prohibits the payment of bribes to foreign officials. In addition to the payment of bribes to foreign officials being a criminal act for U.S. companies, the bribes paid, naturally, cannot be deducted as costs for tax purposes. Many U.S. competitors from other advanced industrialized countries do not have to deal with the same limitations.

More recently a greater sense of urgency over corruption has gripped the United States. Corrupt countries often tend to be failed states and present a series of potential and real problems. These countries pose a threat to the U.S., not from an adversarial power position, but from weakness and inability to control what happens inside their own borders. In those states and others like them—Afghanistan, Somalia, Liberia and Sudan—where internal control has been lost, it is often Americans who pay the price.[6] Iraq was a failed state of a different sort, but still riddled with corruption. In fact, a broad band of weak and failed states—in the greater Middle East, as well as from South and Central Asia to African and the Caribbean—can harbor terrorists and drug traffickers, and spark humanitarian disasters. Ironically, these weak and ineffectual states have the ability to undermine global economic growth and prosperity.[7]

These realities hit home with the September 11th attacks. At that time it became all to apparent to U.S. policymakers that the lack of democracy and freedom, economic stagnation and widespread unemployment—all caused directly, or indirectly by corruption were driving many young people in the Middle East and North Africa towards extremism and terrorism. The World Bank concurs, identifying corruption as the single biggest obstacle to economic development. The World Bank estimates corruption-related activities reduce world income by around five percent or more than $1.5 trillion a year.[8]

In many Middle East countries, corruption has become endemic.[9] The existence of pro-American, yet autocratic regimes in the region no longer guarantees lasting stability or even prosperity. Many of the region's oil

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[6]Stuart Eizenstat and John Edward Porter, "Weak States are a US Security Threat," *Christian Science Monitor,* June 29, 2004, p. 9.

[7]Ibid.

[8]Pedro de la Lata, "Cost of Corruption at $1.5 trillion a year: Experts," *Oman Daily Observer,* December 12, 2003.

[9]"Greater Middle East Partnership," working paper, *Al-Hayat,* February 13, 2004; *Arab Gateway,* February 2004, <http://www.al-bab.com/arab/docs/international/gmep2004.htm>.

states for example have found that resources alone do not produce stability or prosperity. In these economies, the potential for instability created by corruption, often finds its source in weak institutions, the absence of government procurement and auditing systems and a lack of revenue transparency.[10]

In a speech on November 7, 2003, President Bush summed up his Administration's assessment of the region: "As long as the Middle East remains a place where freedom does not flourish it will remain a place of stagnation, resentment and violence easy for export. And with the spread of weapons that can bring catastrophic harm to our country and to our fiends, it would be reckless to accept the status quo."[11]

In this regard, the adoption of the United States' sponsored Broader Middle East and North African Initiative (a later version of the Greater Middle East and North African Initiative) by the Group of Eight Industrialized Nations (G-8) at their June 8-10 summit in Sea Island, Georgia is seen by the Bush Administration as representing a milestone in the war on terrorism. The initiative has two key elements. The first is the launching of a "Partnership for Progress and a Common Future with The Region of the Broader Middle East and North Africa." The second is a plan for the G-8 countries to support reform in Arab countries.

While the G-8 declaration (as well as earlier drafts) commit to "work with governments and business leaders to promote entrepreneurship, expand trade and investment, increase access to capital, support financial reforms, secure property rights, promote transparency and fight corruption,"[12] the details of the initiative are unclear at this time perhaps because of the sensitivity of the issue.

To help appreciate the importance of the corruption issue, together with providing some sense of the factors that contribute to it in the Middle East and North African (MENA) countries, the following sections examine corruption in the region from an empirical perspective. What are the main patterns of corruption in the region? The effect of corruption on the economies? The impact that effective reforms and anti-corruption programs are likely to have on corruption? Based on this analysis a final sec-

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[10]Manuel Paulo and Alex Vines, "Blessing or Curse," *The World Today*, 60:5, May 2004, pp. 26-27.

[11]Quoted in "Bush: West Erred in Tolerating Mideast Corruption," *CNN*, November 7, 2003, <http://www.cnn.com/2003/ALLPOLITICS/11/07/bush.mideast.ap/>.

[12]*Broader Middle East/North Africa Partnership* (Washington D.C.: The White House, June 9, 2004), <http://usinfo.state.gov/xarchives/display.html?p=washfile-english&y=2004 &m=June&x=20040609185638liameruoy0.5483144&t=xarchives/xarchitem.html>.

tion draws some tentative conclusions for possible U.S. anti-corruption initiatives in the region.

Corruption–Conceptual Issues

While many varied definitions exist, the most popular and simplest definition of public corruption is that it is the abuse of public power for private benefit. This is the definition used by the World Bank.[13] Within this framework, acts of corruption cover a spectrum of activities ranging from:
- Bureaucratic (or "petty") or political (or "grand"); for example, corruption by the bureaucracy or by the political leadership.
- Cost-reducing (to the briber) or benefit enhancing.
- Briber-initiated or bribee-initiated.
- Coercive or collusive; centralized or decentralized.
- Predictable or arbitrary; and involving cash payments or not.[14]

Defining corruption is one thing, measuring it is quite a different matter. Even if accurate data simply measuring bribes paid existed, it still would ignore many corrupt practices of a more qualitative nature–tit for tat type acts for example. In actual practice, researchers of corruption issues usually rely on indirect measures of its prevalence in a country or institution.

In this regard, questionnaire-based surveys of corruption perception (not actual measures of corruption) are probably the most realistic measures available. The best known of these surveys, the *Transparency International Index*, for example, assesses the perception of corruption on a scale of 0 to 10. Ten refers to a corruption-free country. Zero refers to a country where most transactions or relations are tainted by corruption. The variance of these indexes, which reflects how the views vary between respondents, is also important in assessing the figures on any individual country. The latest *Transparency International Index* for 2003 shows that of the MENA countries, Oman and Bahrain score the highest and are ranked 26th and 27th respectively. Another cluster of Gulf States, Qatar, Kuwait and the UAE come in at 32, 35 and 37th respectively. Many, beginning with Syria at 66th fall toward the bottom of the rankings.

The World Bank *Control of Corruption Index* is also a perception-driven

[13]Cf. Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, *Governance Matters III: Governance Indicators for 1996-2002* (Washington: The World Bank, June 30, 2003), p. 4.

[14]Vito Tanzi, "Corruption Around the World: Causes, Consequences, Scope, and Cures," *IMF Staff Papers* 45:4 (December 1998). p. 565.

measure. It is derived from a series of sources[15] and is part of a larger data set covering six main areas of governance—control of corruption, voice and accountability, political stability, regulatory quality, rule of law and government effectiveness.[16] The index has a mean of zero, with higher values indicating a greater control of co-option.

Patterns of Corruption in the MENA Region

Using this measure the MENA countries conveniently fall into several distinctive groups (Table 1), with most countries moderately above or below the norm for the world as a whole. Compared with other parts of the world progress at governance reform in the MENA region has lagged somewhat. The MENA countries are:
- somewhat below the norm (-0.151) for control of corruption;
- considerably below other countries in voice and accountability (-0.906);
- lagging in political stability (-0.334), regulatory quality (-0.334) and government effectiveness (-0.196), and
- near the norm with regard to the rule of law.

Most MENA countries are fairly consistent in their reform efforts, either making fairly decent progress across the six main governance measures, or lagging behind across the board. The main exception is voice and accountability, where progress is consistently behind that made in other areas of governance.

With the exception of rule of law, most MENA countries have made improvements in their governance in recent years. However, progress has not been even and a gap may be widening between those countries above the corruption norm, in most measures making relatively more progress, than those below the norm.

Transparency International contends that corruption in MENA countries ultimately stems from the fact that the region is deficient in the two areas necessary for control of corruption—regulatory quality and voice and accountability. With regard to regulatory quality, there has been a tendency for institutional reforms accompanying economic liberalization pro-

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[15]Cf. Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, *Governance Matters III: Governance Indicators for 1996-2002* (Washington: The World Bank, June 30, 2003), p. 97.
[16]The complete data set and description of the measures can be found at: <www.world-bank.org/wbi/governance/govdata2002/>.

grams to lag. Underdevelopment of regulatory powers has created new opportunities for rent seeking. For example, when granting private licenses for providers of mobile phone networks authorities in several countries failed to put in place impartial and effective regulators. According to *Transparency International* the result was wide levels of discretionary powers enjoyed by private providers and state officials—an environment conducive to corruption.[17]

The prevalence of authoritarian rule (lack of voice and accountability) in the region constitutes a hindrance to transparency and accountability at both the state and private levels. Lack of accountability often means state budgets are insufficiently itemized to permit close scrutiny, while important state revenues are managed in extra-budgetary funds or parallel institutions that allow for discretionary spending. Libya's oil revenues, for example, constituting 95 percent of the nation's exports, are held in secret funds and controlled exclusively by Colonel Muammar al-Qaddafi and his associates. Furthermore, most MENA governments compensate for low popular support or poor legitimacy by granting opportunities for bribery to leading families or cliques.[18]

Clearly the installation of democratic institutions would help in promoting accountability, but given the long history of corruption in the region, it would probably not be sufficient to eradicate corruption, at least in the short term. At a minimum, to accomplish this, better regulatory structures would have to be put in place in most countries as well as further strengthening of the rule of law. Even with reforms in these areas, old habits are likely to die hard—no doubt it will take some time before the cycle of corruption is broken in many of the MENA countries.

Corruption Linkages

A crude plot of per capita income and *Transparency International's* Corruption Perceptions Index—CPI (Figure 1), suggests that with growth, rising incomes and awareness on the part of the population at large will place enough pressure on governments to undertake the necessary reforms. Perhaps, countries just naturally outgrow their need for and tolerance of corruption.

After years of study, economists have concluded that a country's ability

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[17]Reinoud Leenders and Hohn Sfakianakis, "Middle East and North Africa," in *Transparency International.*
[18]Ibid.

to accumulate physical and human capital and the efficiency with which it turns its capital and natural resources into goods and services are key factors in explaining differences in national incomes. Another truism is that to attain high rates of capital formation, investors require legal protection. In this regard, countries adhering to common law generally have the strongest legal protection for investors, followed by counties adhering to civil law adopted from the German and Scandinavian legal traditions; many MENA countries rooted in French civil law offer the weakest legal protection.[19]
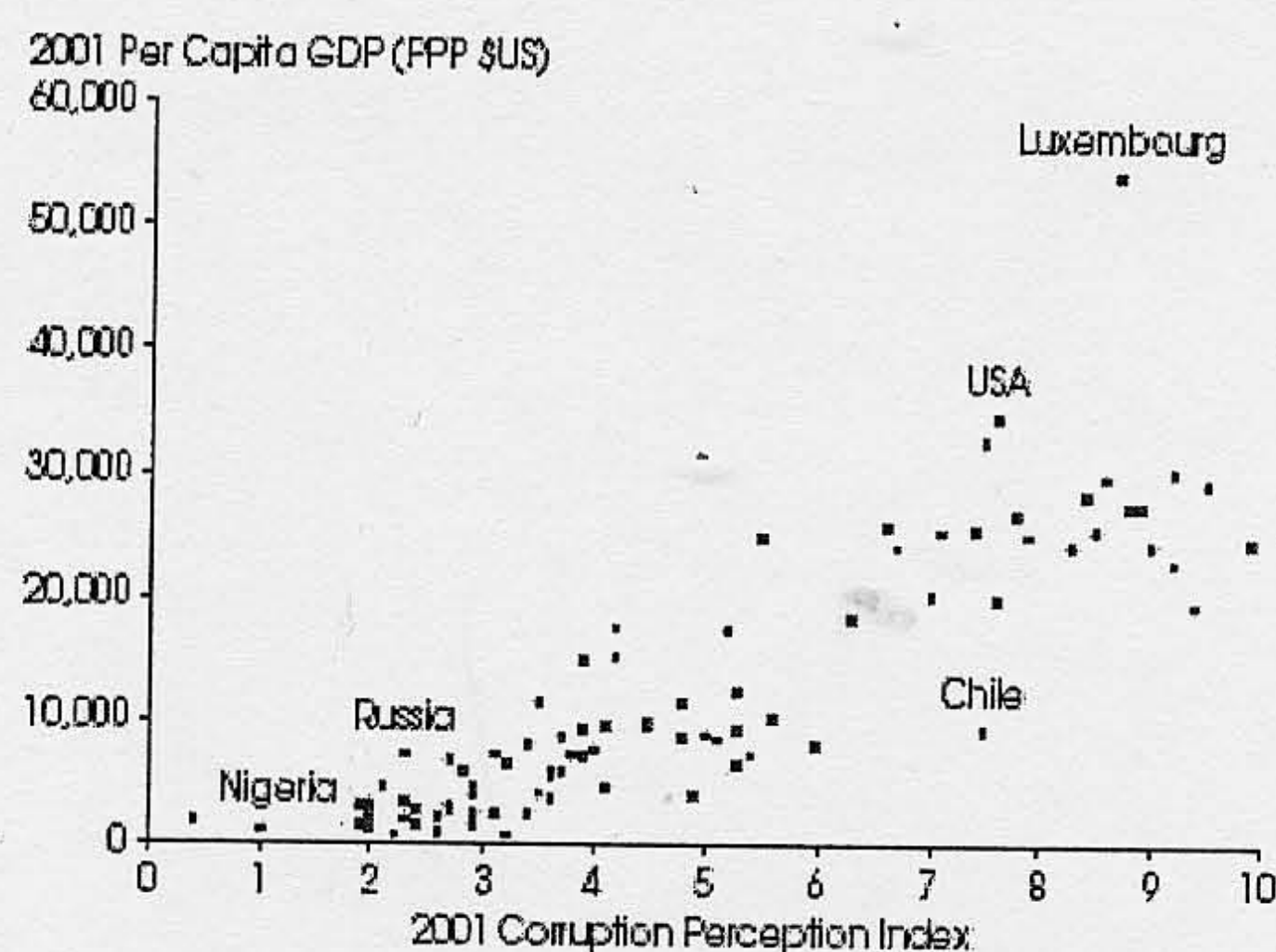
SOURCES: United Nations Human Development Report 2003, http://hdr.undp.org/reports/global/2003. Global Corruption Report 2001, http://www.globalcorruptionreport.org.

Figure 1
Corruption Perception Index and Per Capita Income

Legal systems that provide strong protection for investors have permitted the development of sophisticated financial markets, which enhances the economy's ability to bear risk. This ability to spread risk over a multitude of investors is critical for entrepreneurship and economic growth. However, differences in legal systems are only part of the story. Actual enforcement of the law is equally or even more important. The absence of enforcement enables corruption to render codified law ineffective. When laws are not enforced, corruption is able to weaken property rights and

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[19]Rafael La Porta, Florencio Lopez-deSilanes, Andrei Shleifer and Robert Vishny, "Law and Finance," *Journal of Political Economy* 106:6 (December 1988), pp 1113-55.

deprive investors of compensation for risk taking and increase the uncertainty about potential investment payoffs. This decreases the incentive to invest, which in turn dampens economic growth.[20]

Another detrimental aspect of corruption is its tendency to distort markets. In turn, market distortion results in an inefficient allocation of resources, which further reduces wealth creation and growth.[21] Specifically corruption:

- **Undermines the market system.** Corruption often reduces the ability of the government to impose the necessary regulatory controls and inspections to correct market failures –a situation where social costs and benefits differ from private ones.[22] The result often is reflected in rates of investment and output. Similarly when corrupt governments create exploitative monopolies for private interests, investment and output most always decline.
- **Distorts incentives.** In a corrupt environment, able individuals often tend to find it more profitable to apply their energies to rent seeking–the pursuit of artificially high profits created through the granting of special licenses, quotas and other restrictions on market supply–instead of focusing on production or innovative activity. In these cases there is usually more money to be made in collecting rents than in actually producing the goods themselves.
- **Creates inefficient industries.** In some instances governmental protection from foreign competition has actually encouraged the growth of local firms with negative value added, thus reducing national output.[23]
- **Acts as an arbitrary and uncertain tax.** Corruption's capricious nature creates high excess burdens as the cost of searching for the right person to bribe must be added to the cost of negotiating and paying the bribe.
- **Weakens financial system.** Because the size of the bribe is often unclear, excessive cash balances must be kept, thus reducing the

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[20]Jason Higbee and Frank Schmid, "Rule of Law and Economic Growth," Federal Reserve Bank of St. Louis, *International Economic Trends* (August 2004).

[21]Vito Tanzi, "Corruption Around the World: Causes, Consequences, Scope, and Cures," *IMF Staff Papers* 45:4 (December 1998), pp. 583-84.

[22]R.H. Coase, "The Problem of Social Cost," *Journal of Law and Economics* 3 (1960), pp. 1-44.

[23]The case of Pakistan is vividly illustrated in Stephen R. Lewis, *Pakistan: Industrialization and Trade Policies* (London: Oxford University Press, 1970).

funds available from the financial system for productive investment—in a corrupt economy a preponderance of transactions are in cash.

Finally corruption is likely to increase poverty because it reduces the income earning potential of the poor. This effect stems from the fact that enterprises can protect themselves more easily from corrupt officials because:

- They have specialized departments that can deal with aggressive bureaucrats.
- They can use "facilitators" individuals skilled at fighting through the jungle of opaque regulations and tax laws.
- Their size makes them more immune to the extortion of petty bureaucrats.

In turn the poverty created and maintained by corruption inhibits growth through the underdevelopment of large domestic markets.[24]

The Empirical Dimension

These general propositions concerning the adverse impact of corruption on incomes and growth have been confirmed in numerous empirical studies[25] where it was found that corruption:

1. **Reduces investment** and as a consequence reduces the rate of growth. Such reduction in investment is assumed to be caused by the higher costs and the uncertainty that corruption creates.[26]
2. **Reduces expenditure on education and health**, because these allocations do not easily lend themselves to corrupt practices on the part of those who make budgetary decisions. Since human capital has been found to be one of the main sources of long-term economic growth, a major cost of corruption is this foregone income.
3. **Increases public investment** because public investment projects lend themselves to "kick-backs." A related "White Elephant" effect is notorious for diverting capital from more productive private sec-

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[24]Vito Tanzi, "Corruption Around the World: Causes, Consequences, Scope, and Cures," *IMF Staff Papers* 45:4 (December 1998), pp. 583-84.

[25]Ibid.

[26]Paolo Mauro, "Corruption and Growth," *Quarterly Journal of Economics* 110 (August 1995), pp. 681-712.

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4. **Increases the acquisition of weapons systems** where large "commissions" often accrue to the cronies of local officials. Empirical evidence suggests that often the link between military expenditure and income growth is negative.[27]

5. **Reduces expenditure for operation and maintenance** since the normal budgetary process makes corruption more difficult than in the case of normal procurement. The effect is to lower the productivity of public capital, slowing private investment thus producing a drag on economic growth.

6. **Reduces tax revenue** directly where bribes are paid for tax avoidance. If governments run deficits to offset the loss of revenue, the ensuing inflation may distort and retard the pattern of investment.

7. **Reduces foreign direct investment** because corruption has the same effect as a tax. The less predictable the level of corruption (the higher is its variance) the greater its impact on foreign direct investment.

Corruption and Per Capita Income in the MENA Region

The previous sections suggest that improving the control of corruption is likely to be a productive way to initiate sustained growth in the MENA region. Logically these benefits would be even greater for those countries below the norm on the World Bank's *Control of Corruption Index*. However improvement in other areas of governance such as voice and accountability may, from an empirical perspective have even a greater positive impact on the economy. The same could be said for improvements in the rule of law, or for that manner any of the other main areas of governance.

Generalizations of this type for the region are a bit difficult because the governance and economic structures of MENA countries vary considerably depending on whether or not they are oil exporters. These considerations are especially important in the context of corruption—the nature or types of corruption found in the oil countries (rentier economies) varies considerably from that commonly found in the non-oil economies.[28]

In the case of the oil-exporters, especially the oil monarchies and emirates of the Gulf, the ruling families have in large part appropriated the

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[27]Robert Looney, "Budgetary Dilemmas in Pakistan," *Asian Survey* XXIV:5 (May 1994).

[28]Amity Shlaes, "In Poorer Nations, Oil Resources Can Be a Curse Upon the People," *Los Angeles Times*, June 21, 2004, B9.

profits from the oil sector through blurring the distinction between public and private treasure and extending their familial involvement beyond oil to include local industry, services and trade, through public and private contracting.[29] Since a great deal of this is internal, with foreign investment often frozen out of a wide spectrum of industries, much of this type of corruption may slip by the standard corruption perception surveys.

On the other hand, many of the non-oil MENA countries have the remnants of former state-run socialist economies. Despite some economic liberalization and privatization in the past couple of decades, high government officials still have supreme control over the economic resources of the country. They not only control the massive public sector but they also dominate the private sector in that much of the private sector is dependent on contracts or cooperation from the public sector to undertake its business. "Government elites that trace their routes to austere military backgrounds or political parties, have mellowed into traditional power holders who place their children and relatives in positions of power and profit and seek to translate their political authority into financial and economic power as well."[30]

Differences Between Rentier and non-Rentier MENA Economies

Some of the differences in the environments of rentier and non-rentier MENA countries are reflected in their varied progress in governance and economic reforms. With the exception of the rule of law, the MENA countries as a whole score considerably below non-MENA states in all of the standard measures of governance. The gap is largest for voice and accountability. Within the MENA countries the rentier states score below the non-rentier states in voice and accountability and regulatory quality. On the other hand the rentier economies have considerably more political stability and less corruption, at least as revealed by the perception surveys. Rule of law is firmer in the rentier economies as is government effectiveness.

In the economic area (high values reflect lower attainment) the MENA countries lag behind the non-MENA states considerably in trade policy, fiscal burden, government intervention, foreign investment, banking and finance, wages and prices and property rights. The MENA states have had

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[29]Paul Salem, "The Impact of Corruption on Human Develop in the Arab World: A Concept Paper," (New York: United Nations Development Program, April 2003).
[30]Ibid.

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more progress in monetary policy, and regulation. Both groups are about even in controlling the informal market. There is no doubt that the generally low regulatory quality in the MENA countries, the protection from foreign trade and limited government effectiveness and large scale government intervention provide a fertile environment for corruption to flourish. This is only reinforced by the huge MENA deficit in voice and accountability.

Within the MENA region, the rentier countries have had more economic liberalization in the trade area, but their governments tend to intervene considerably more than in the case of the non-rentier states. The non-rentier countries have created a much more favorable environment for foreign investment. They have also liberalized their markets to a greater extent than the rentier states.

Empirical Links Between Corruption and Per Capita Income

As noted above, the differences in governance and economic freedom between MENA and Non-MENA countries as well as those between the MENA rentier and non-rentier economies will likely affect the manner in which a certain level of corruption impacts on an individual country's economy. For the broad groupings of countries a statistical analysis[31] suggests that the plot diagram in Figure 1 is somewhat misleading. While the correlation between the two variables in the diagram is around 0.87 and highly significant statistically, other variables play an important role in effecting incomes. In addition, other groupings of countries paint quite a different picture.

Specifically, while control of corruption is a major determinant of per capita income for a large sample of developing countries (125), it is not as important a factor as the improvement of over-all governance (an average of the six governance measures under examination). Whether or not a country was a rentier economy also positively affects per capita income. That is everything else equal, rentier economies have a higher per capita income than non-rentier economies. Finally, the share of capital formation in GDP also positively affects per capita income.

These results change dramatically if the sample of countries is confined to those with per capita incomes under $1,000. For these countries capital formation as a share of GDP was the only statistically significant variable

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[31]The results are available from the author upon request at <relooney@nps.edu>.

affecting per capita income. In other words, in and of itself, improvements in the control of corruption (or any other governance variable for that matter) would not advance a country's per capita income.

For countries with per capita incomes greater than $1,000, control of corruption was the major determinant of per capita incomes. Again, given a rate of control of corruption, whether or not a country was a rentier economy affected per capita income with the rentiers attaining higher income levels.

It's interesting to note that control of corruption was the most significant variable affecting per capita income in both the MENA[32] and Non-MENA groups of countries. The major difference between the two groups was the presence of the rentier effect in the MENA sample, but not in the Non-MENA group of countries. For the non-MENA countries, improvements in the rule of law impacted positively on per capita incomes. This was not the case for the MENA states.

In short these findings support the argument that control of corruption is a major factor affecting per capita income. However, over time improvements in per capita income will no doubt affect the ability and willingness of nations to fight corruption. While there may be real world exceptions, these results appear to apply to countries with per capita incomes already over $1,000. Unfortunately, these countries are often those who are the most deficient in all areas of governance. Perhaps one reason for the lack of reforms in these countries is the absence of immediate income gains to show for the sacrifices accrued.

As suggested above, many countries that have achieved excellent progress in improving their governance have also made commensurate gains in reforming many key areas of economic policy. It is possible therefore that per capita income is really more related to economic reform rather than governance improvements. In this case the apparent association between improvements in the control of corruption and higher per capita income would be spurious. Additional tests were undertaken to check for this possibility.

The results (Table 2) basically confirm the importance of the control of corruption as a major factor affecting per capita incomes—this variable is still statically significant in affecting per capita incomes in both the MENA and non-MENA groups of countries after explicitly taking into account economic reforms. Of the economic variables, improvements in the fiscal

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[32]Because of the small number of rentier economies (10) within the MENA group, meaningful statistical analysis of the difference in MENA rentiers and non-rentiers was impossible.

burden is likely to have a positive impact on MENA per capita incomes, while improved trade policy is associated with higher per capita incomes in the non-MENA countries.

Improvements in the Control of Corruption on Other Areas of Reform

As suggested above, it is unlikely that the various aspects of governance and economic freedom are completely independent of each other—progress in one area is likely to affect the willingness of policy makers in pressing ahead with similar reforms in other areas. Given that progress in all reforms is a desirable outcome, it's of some interest to identify the extent to which anti-corruption drives have this carry over effect. As a basis of comparison, the analyses also included the overall-index of economic freedom along with the corruption index.

The results (Table 3) suggest that anti-corruption efforts lead to somewhat different outcomes in the MENA countries than in the non-MENA countries. Most importantly, there appear to be many more reform linkages in the non-MENA group. While in both groups of countries, improvements in anti-corruption carry over to improvements in all of the other areas of governance, the non-MENA countries also experience many similar positive effects from improvements in economic freedom. Improved economic freedom leads to improved regulatory quality in both sets of countries, but in the case of the non-MENA group, positive changes in voice and accountability, government effectiveness and overall-governance also accrue from improvements in economic freedom.

A similar pattern characterizes the various areas of economic freedom. While both groups of countries experience a number of positive stimuli on individual reform areas stemming from an improvement in their over-all index of economic freedom, the non-MENA countries also experience a similar effect from improvements in their control of corruption. For them, improvements in the corruption area carry over to trade policy, government intervention, monetary policy, property rights, regulation and the informal markets. Trade policy appears to be the only area positively affected by improvements in corruption occurring in the MENA countries.

Factors Affecting Corruption

Finally, anti-corruption initiatives are likely to be affected by develop-

ments (positive or negative) in the various areas of governance and or economic freedom. For the non-MENA countries (Table 4), improved government effectiveness appears to carry over to positive action in the control of corruption. For these countries, improved voice and democracy also appear important in this regard. In contrast, improvements in over-all economic freedom and political stability appear to be the critical areas of improvement leading to improvements in the control of corruption. In other words the non-MENA countries appear to undertake anti-corruption measures via a more democratic political process that utilizes the pressure from a more efficient governmental structure to eliminate corruption. In the MENA countries, political stability appears to be critical for anti-corruption efforts. In this context, it is possible to view anti-corruption efforts as a necessary component in maintenance of gains in economic freedom.

This model predicts well over 90 percent of the differences in corruption throughout the MENA region (bottom, Table 4). As one might anticipate, there is a slight tendency for it to under-predict the corruption in the higher corruption countries and to over-predict it in the case of the lower corruption countries.

Assessment

On both conceptual and empirical grounds, a strong case can be made for giving corruption a high priority in the MENA region. Improved control of corruption appears critical for moving up the per capita income ladder. Given the political dynamics in the region, efforts in the realm of corruption appear to pay high dividends by inducing improvements in other areas of governance, especially voice and accountability, political stability, government effectiveness, and to a lesser extent regulatory quality. Unfortunately, an improved corruption environment does not appear to significantly stimulate carry-over reforms in the economic realm.

Clearly its problematic the extent to which reforms can or should be encouraged by countries outside the region. A group of first class Arab minds, the Project for Democracy Studies in Arab Counties, has stressed the importance of indigenously initiated reforms:

> The sense of managing alone contrasts sharply with the attitude of most Arab commentators, who delight in blaming the rest of the world for every misfortune, real or imagined, and look to right all wrongs. The Oxford delegates believe that it is only

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[33]Mai Yamani, "The Middle East's Lost Resources: Arab Blues at Oxford," *International Herald Tribune*, September 3, 2004.

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Arabs themselves who can create the institutions in their societies that can lead them to a better future.[33]

To a certain extent, the basis for an indigenous reform process may already exist in many of the key MENA countries. As noted above, in the MENA region, control of corruption appears to improve with increases in the over-all economic freedom score as well as improvements in political stability. The economic freedom index is a composite of the various categories—foreign investment, trade policy, banking and finance and the like.

Given that improvements in the corruption situation in the MENA countries do not appear to stimulate carry-over economic reforms, there may be a very positive role for countries outside the region to play. The United States' direct approach of trying to speed up the democratization process so far has resulted in increased political instability in some of the countries in the region. However, through international organizations, such as the IMF and the WTO, the United States can play an active role in supporting reforms—for example, trade liberalization to comply with WTO agreements. Perhaps, the most effective path for the U.S. to take may well be an indirect multilateral one.

Table 1
MENA Economies: Summary Statistics on Governance Indicators
(Average 1996-2002)

Country	Voice Accountability	Regulatory Quality	Political Stability	Government Effectiveness	Rule of Law	Control of Corruption
Highly Corrupt Countries (Corruption Index < -0.75)						
Iraq	-1.953	-2.923	-2.213	-1.626	-1.590	-1.315
Libya	-1.563	-2.084	-0.920	-1.103	-0.967	-0.876
Sudan	-1.684	-1.148	-2.238	-1.385	-1.295	-0.994
Average	-1.733	-2.051	-1.790	-1.371	-1.284	-1.061
Fairly Corrupt Countries (Corruption Index >-0.75<0.0						
Algeria	-1.209	-0.799	-2.093	-0.746	-0.677	-0.590
Egypt	-0.803	-0.092	-0.167	-0.081	0.178	-0.154
Iran	-0.912	-1.394	-0.292	-0.310	-0.558	-0.599
Lebanon	-0.456	0.117	-0.430	-0.132	-0.114	-0.339
Syria	-1.522	-0.955	-0.276	-0.796	-0.371	-0.568
Turkey	-0.607	0.391	-0.923	-0.162	0.070	-0.154
Yemen	-0.768	-0.525	-1.278	-0.632	-0.946	-0.549
Average	-0.896	-0.465	-0.779	-0.408	-0.345	-0.421
Less Corrupt Countries (Corruption Index >0.0<0.75)						
Bahrain	-1.007	0.863	-0.032	0.563	0.860	0.448
Jordan	-0.235	0.340	0.056	0.375	0.422	0.059
Morocco	-0.468	0.156	-0.059	0.083	0.289	0.108
Oman	-0.635	0.578	0.915	0.877	1.104	0.689
Qatar	-0.720	0.307	1.141	0.721	1.060	0.598
Saudi Arabia	-1.298	-0.039	0.154	-0.106	0.670	0.174
Tunisia	-0.740	0.282	0.499	0.803	0.314	0.279
UAE	-0.611	0.690	0.963	0.584	1.096	0.702
Average	-0.714	0.397	0.454	0.487	0.726	0.382
Relatively Uncorrupt Countries (Corruption Index > 0.75)						
Kuwait	-0.255	0.048	0.438	0.142	0.943	0.901
Total Av	**-0.906**	**-0.334**	**-0.372**	**-0.196**	**0.002**	**-0.151**

Source: Compiled from: Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, Governance Matters III: Governance Indicators for 1996-2002, (Washington: World Bank, June 30, 2003).

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Table 2

Effects of Governance and Economic Freedom Reforms on Per Capita Income

Independent Variable	Standardized Coefficient	t statistic	significance	Adjusted R square

Dependent Variable: Average Per Capita Income 1995-2002–Purchasing Power Parity $1995

(1) Developing Countries Sample (df =121)

Independent Variable	Standardized Coefficient	t statistic	significance	Adjusted R square
Rentier Dummy	0.233	4.596	0.000	0.668
Regulation	-0.250	-3.241	0.002	0.683
Capital Formation (% GDP)	0.166	3.320	0.001	0.692
Control of Corruption	0.494	6.660	0.000	0.701
Trade Policy	-0.161	-2.804	0.006	0.698

(2) Countries with Per Capita Income Greater than $1,000 (df =128)

Independent Variable	Standardized Coefficient	t statistic	significance	Adjusted R square
Control of Corruption	0.786	14.631	0.000	0.781
Trade Policy	-0.135	-2.501	0.014	0.791
Rentier Dummy	0.154	3.194	0.002	0.798
Primary Producer Dummy	-0.109	-2.204	0.029	0.804

(3) Countries with Per Capita Income Greater less than $1,000 (df =18)

Independent Variable	Standardized Coefficient	t statistic	significance	Adjusted R square
Capital Formation (%GDP)	.470	2.193	.042	.175

(4) MENA Countries (df =16)

Independent Variable	Standardized Coefficient	t statistic	significance	Adjusted R square
Fiscal Burden	-0.393	-4.100	0.001	0.698
Control of Corruption	0.432	4.986	0.000	0.862
Rentier Dummy	0.320	3.574	0.003	0.925

(5) Non-MENA Countries (df =130)

Independent Variable	Standardized Coefficient	t statistic	significance	Adjusted R square
Control of Corruption	.807	14.961	.000	.798
Trade Policy	-.129	-2.396	.018	.806
Capital Formation (% GDP)	.083	2.180	.031	.811

Notes: Stepwise Regression with all variables entered initially. Independent variables = rentier dummy, primary producer dummy, capital formation (% GDP). Independent governance variables: voice and accountability, political stability, government effectiveness, regulatory quality, rule of law, control of corruption, overall governance (average of governance measures). Economic freedom variables: trade policy, fiscal burden, government intervention, monetary policy, foreign investment, banking and finance, wages and prices, property rights, regulation, black markets. Non-dummy variables are averages over the 1996-2002 period for governance and 1995-2002, economic freedom. Governance data from: Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, Governance Matters III: Governance Indicators for 1996-2002, (Washington: World Bank, June 30, 2003). Index of Economic Freedom Rankings, (Washington: Heritage Foundation), various issues).Capital formation share of GDP–World Development Indicators 04 CD-ROM (Washington: World Bank 2004).

Table 3
Impact of Anti-Corruption and Economic Reforms on Governance and Economic Freedom

Reform Area	Over $ 1,000 per-Capita Income		MENA Countries		non-MENA Countries		Rentier Economies	
Governance Measures								
Voice, Accountability	CORR	EF	CORR		CORR	EF	CORR	
Political Stability	CORR		CORR		CORR		CORR	
Govt. Effectiveness	CORR	EF	CORR		CORR	EF	CORR	
Regulatory Quality	EF	CORR	EF	CORR	EF	CORR	EF	
Over-All Governance	CORR	EF	CORR		CORR	EF	CORR	
Economic Freedom								
Trade Policy	EF	CORR	CORR		EF	CORR	CORR	
Fiscal Burden	CORR	EF	EF		CORR	EF	EF	
Govt. Intervention	EF	CORR			EF	CORR	EF	
Monetary Policy	EF		EF		EF	CORR	CORR	
Foreign Investment	EF		EF		EF		EF	CORR
Banking & Finance	EF		EF		EF		EF	
Wages & Prices	EF		EF		EF			
Property Rights	CORR	EF	EF		EF	CORR	EF	
Regulation	EF	CORR	EF		EF	CORR	EF	
Informal Market	CORR	EF	EF		CORR	EF	CORR	EF

Notes: CORR = Average corruption index 1996-1998, EF = average economic freedom score, 1995-1999. Governance and Economic Freedom Measures = average scores, 2000-2002. Only statistically significant results reported. In all cases for the statistically significant variables, EF and CORR, improvements result in a positive impact on the respective governance, economic reform index.

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Table 4

Effects of Governance and Economic Freedom Reforms on Corruption

Independent Variable	Standardized Coefficient	t statistic	significance	Adjusted R square

Dependent Variable: Corruption Index (Average 2000-2003)

Non-MENA Countries

Government Effectiveness	.832	19.516	.000	.883
Rentier Dummy	.110	3.951	.000	.888
Voice, Accountability	.164	3.681	.000	.897

MENA Countries

Rentier Dummy	.234	4.526	.000	.885
Economic Freedom Index	-.483	-7.417	.000	.950
Political Stability	.561	8.589	.000	.952

MENA Country	Actual Corruption	Predicted	Actual-Predicted Scores
Higher Corruption Countries			
Algeria	-0.673	-0.742	0.069
Egypt	-0.237	-0.213	-0.024
Iran	-0.497	-0.347	-0.149
Iraq	-1.315	-1.317	0.002
Lebanon	-0.433	-0.116	-0.316
Libya	-0.880	-0.867	-0.012
Sudan	-1.112	-1.240	0.128
Syria	-0.518	-0.453	-0.064
Turkey	-0.341	-0.234	-0.106
Yemen	-0.697	-0.798	0.101
Average	-0.670	-0.633	-0.037
Lower Corruption Countries			
Bahrain	0.655	0.778	-0.123
Jordan	0.061	0.153	-0.092
Kuwait	0.971	0.727	0.243
Morocco	0.162	0.037	0.124
Oman	0.875	0.764	0.110
Qatar	0.821	0.732	0.088
Saudi Arabia	0.326	0.473	-0.147
Tunisia	0.522	0.271	0.250
UAE	0.925	1.005	-0.081
Average	0.591	0.550	0.041
Total MENA Averages	-0.073	-0.073	0.000