

When Business Finds the Right Sort of Corruption Congenial

By Hilton L. Root

MANILA — The arrest of Roh Tae Woo, South Korea's former president, for raising \$650 million in corporate contributions for a personal slush fund has made worldwide headlines. The reputations of political parties in Japan, Malaysia and Taiwan have similarly been tarnished by scandal. Why has corruption, an impediment to attracting capital elsewhere, not held back East Asia's high-performing economies?

Business people insist that venality increases business risk and uncertainty. Why then does it not drive investors away from East Asia?

To see why graft in the region does not have a debilitating impact on economic confidence, consider one of the most irksome sources of uncertainty in business calculation — a capricious and opaque regulatory environment.

In many developing countries, bureaucratic posts with limited salary are typically awarded to political followers. Politicians then will look the other way when their supporters abuse public responsibilities to enrich themselves from state coffers.

Once the bureaucracy is bloated with political appointees, the pool of money available for salaries shrinks, increasing the appeal of non-salary supplements. Patents, licensing, local regulatory codes, import-export schedules and tax programs all provide opportunities to use public office for private enrichment.

Business has no way to anticipate the resulting uncertainty, delays and unforeseen expenditures from manipulation by the gatekeepers of an opaque regulatory regime as bureaucrats become specialists in the multiplication of nuisances that only they can contain.

Contrasted with kump-sum, up-front payment to a political party, which can be anticipated and amortized, this kind of graft causes apprehension because the investor never knows where the next demand will come from or how much will be requested.

Reducing the costs often associated with bureaucratic venality is the first clue to the puzzle of why political corruption in South Korea did not impair investment. The administrative reforms of the late President Park Chung Hee eliminated many of the sources of bureaucratic abuse.

Administrative structures in South Korea are highly centralized, and licensing for large investments is dominated by a single agency that reports directly to the president. Merit, not patronage, is the basis of recruitment and promotion within the bureaucracy; independent boards that administer exams determine bureaucratic career paths.

Despite the growth of venality at all levels of the South Korean political system, the administrative mechanisms introduced and institutionalized by General Park have hardly changed and are not implicated in the current scandals.

Another potential source of business uncertainty is unstable macroeconomic, monetary and trade policy. Companies are persuaded to support the dominant incumbent political party in South Korea to ensure the continuity of policies that promote capital investment.

In effect, when business people give money to political parties, they do so to ensure regulatory benefits and policy outcomes that they value, and to prevent something that they don't like — sudden, unpredictable changes in the rules of the game that can devastate investors in any country.

Although democracy is linked in many minds with greater government accountability, politicians extract more money from business in South Korea as democratic institutions are consolidated. Why does policy stability cost more with democracy?

Opposition parties may offer an altered policy mix that may not be favorable to business.

They might also change the application of rules and regulations. Economic regulations in developing countries tend to be very general, inviting new applications that are, in effect, policy alternatives.

To avoid these risks, those in power request more money to keep challengers at bay while inventing innovative ways to raise funds from the firms whose interests would be endangered by a change of regime.

South Korea is an example of the escalating costs of political support during the consolidation of democracy. The structure of government, including presidential oversight of important functions, has changed little since General Park's death in 1979. The president's office still controls the prosecutor's office, police, tax authorities, allocation of credit and major investment projects.

However, because the political system has become more competitive, the party in power can charge more for protection from policy change. This allowed President Roh to amass his secret \$650 million fund from 1988 to 1993. Nothing fundamentally has altered, but a change in party implies the possibility to investors of a change in the rules even after their investments have been made. As a result, more insurance from political uncertainty can be sold.

In South Korea, self-enforcing limits on contributions exist because the Liberal Democratic Party has incentives to keep firms that make capital investments healthy. To secure political survival, the party leadership in turn promotes technocratic guidance of the economy and provides a clean bureaucracy to prevent the dissipation of private sector profits by dozens of side payments. Campaign contributions are part of a system that includes the creation of a business environment conducive to long-term investments.

When political party leaders, rather than a particular politi-