

*The Effects of Corruption  
on the  
Namibian Economy*

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Honorable Prime Minister, Dr Nahas Angula  
Eminent Regional and Local Government Councillors  
Members of Parliament  
Distinguished Guests  
Ladies and Gentlemen

**Corruption - defined as 'the abuse of public power for personal ends' - has always existed in the world.** Corruption has been around for a very long time and is becoming a much more visible and volatile political issue. But increasingly it is also becoming an economic issue. World wide, business people and politicians have been hurled into prisons, prominent executives have been publicly disgraced and Presidents have been impeached because of corruption.

Internationally, the study of the causes and consequences of corruption has a long history in economics, going back 30 years. The classic way corruption became an economic issue is through “rent seeking activities”. For most of the Namibians, rent is what we pay the landlord each month or what a rental agency at an airport charges for letting us use a car for a week. For us as economists, however, rent is short for "economic rent" and means something quite different.

Economic rent is that extra amount paid (over what would be paid for the best alternative use) to somebody or for something useful whose supply is limited either by nature or through human ingenuity. For example, Mike Tyson, the boxing champion, has a natural and rare talent for flooring his opponents during the first round and he was paid some N\$500 million for exercising this talent. If he were not a talented boxer, Mr. Tyson's alternative employment would likely be somewhat more modest, earning, say,

about N\$200,000 a year. The difference that he gets is an economic rent accruing to Mr. Tyson because nature has seen to it that boxers of his skill are in very short supply.

Similarly, for several years during the 1980s the U.S. government restricted the import of Japanese automobiles to a certain quota, creating an artificial shortage of foreign cars. The result? General Motors and other U.S. car manufacturers not only sold more cars but raised their prices, thereby enjoying an economic rent (the difference between the price of domestic cars and the cheaper but unavailable Japanese alternative).

Be that as it may, economic effects of corruption is notoriously hard to measure as it is normally clandestine and its effect is protractive.

**During recent decades, however, corruption has grown both in terms of geographic extent and intensity. Since the mid 1970s, it has infiltrated virtually every country in the world, most notably in Namibia. The "cancer of corruption" has clearly become evident especially in Sub Saharan Africa and economic research shows that corruption can eat away at the fabric of any economy. Economic researchers have also begun to look at quantifying and justifying the presence of corruption through so-called corruption indices, notably by Transparency International, World Economic Forum and here at home Afro-barometer index by the Institute of Public Policy Research.**

### *Sources of Corruption*

But where does corruption originate from in the economy and what in forms does this rent seeking activity takes place. The IMF has identified some key factors in terms of being sources of corruption in any given economy.

\* **Firstly, trade restrictions** are the prime example of a government-induced source of rents. If importing a certain good is subject to quantitative restriction (for example, only so many foreign automobiles can be imported each year), the necessary import licenses become very valuable and importers will consider bribing the officials who control their issue. More generally, protecting a home industry (such as infant industry) from foreign competition through tariffs creates a semi-monopoly for the local industry. Local manufacturers will lobby for the establishment and maintenance of these tariffs and some may be willing to corrupt influential politicians to keep the monopoly going. Studies have shown that a very open economy is significantly associated with lower corruption. In other words, countries tend to be less corrupt when their trade is relatively free of government restrictions that corrupt officials can abuse.

\* Government **subsidies** can constitute a source of rents. Studies show corruption can thrive under industrial policies that allow poorly targeted subsidies to be appropriated by firms for which they are not intended. The more such subsidies are available to industries, the higher the corruption index.

\* **Price controls**, whose purpose is to lower the price of some good below its market value (usually for social or political reasons), are also a source of rents and of ensuing rent-seeking behavior. Price controls create incentives for individuals or groups to bribe officials to maintain the flow of such goods or to acquire an unfair share at the below-market price.

\* **Multiple exchange rate practices and foreign exchange allocation schemes** lead to rents. Some countries have several exchange rates--one for importers, one for tourists, one for investors, for example. Differentials among these rates can lead to attempts to obtain the most advantageous rate, although this rate might not apply to the intended use of the exchange. Multiple

exchange rate systems are often associated with anti-competitive banking systems in which a key bank with government ties can make huge profits by arbitraging between markets. Some countries have little foreign currency and distribute what they have through various schemes, with varying degrees of transparency. If, for example, state-owned commercial banks ration scarce foreign exchange by allocating it according to priorities established by government officials, interested parties may be willing to bribe these officials to obtain more than their fair share.

\* **Low wages in the civil service** relative to wages in the private sector are a source of low-level corruption. When civil service pay is too low, civil servants may be obliged to use their positions to collect bribes as a way of making ends meet, particularly when the expected cost of being caught is low.

\* **Natural resource endowments** (oil, gold, exotic lumber) constitute a textbook example of a source of rents, since they can typically be sold at a price that far exceeds their cost of extraction and their sale is usually subject to stringent government regulation, to which corrupt officials can turn a blind eye. Resource-rich economies may be more likely to be subject to extreme rent-seeking behavior than are resource-poor countries.

\* **Sociological factors** may contribute to rent-seeking behavior. An index of ethnolinguistic fractionalization (societal divisions along ethnic and linguistic lines) has been found to be correlated with corruption. Also, public officials are more likely to do favors for their relatives in societies where family ties are strong.

### *Consequences of Corruption*

Given the sources, what effects does it have on an economy.

\* In the presence of corruption, businessmen are often made aware that an up-front bribe is required before an enterprise can be started

and that afterwards corrupt officials may lay claim to part of the proceeds from the investment. Empirical evidence suggests that corruption **lowers investment and retards economic growth** to a significant extent.

\* Where rent seeking proves more lucrative than productive work, **talent will be misallocated**. Financial incentives may lure the more talented and better educated to engage in rent seeking rather than in productive work, with adverse consequences for the country's growth rate.

\* Of particular relevance to developing countries is the possibility that corruption might reduce the effectiveness of **aid flows** through the diversion of funds. Aid, being fungible, may ultimately help support unproductive and wasteful government expenditures. Perhaps as a result, many donor countries have focused on issues of good governance, and in cases where governance is judged to be especially poor, some donors have scaled back their assistance.

\* When it takes the form of tax evasion or claiming improper tax exemptions, corruption may bring about **loss of tax revenue**.

\* By reducing tax collection or raising the level of public expenditure, corruption may lead to **adverse budgetary consequences**. It may also cause monetary problems if it takes the form of improper lending by public financial institutions at below-market interest rates.

\* The allocation of public procurement contracts through a corrupt system may lead to lower **quality of infrastructure and public services**.

\* Corruption may distort the **composition of government expenditure**. Corruption may tempt government officials to choose government expenditures less on the basis of public welfare than on the opportunity they provide for extorting bribes. Large

projects whose exact value is difficult to monitor may present lucrative opportunities for corruption. A priori, one might expect that it is easier to collect substantial bribes on large infrastructure projects or high-technology defense systems than on textbooks or teachers' salaries.

*Are all these present in Namibia?*

**Remember earlier on, its difficult to measure corruption in Namibia let alone its effects. But there are reports that points to that direction that corruption is indeed present in Namibia. No improvement in corruption situation in Namibia** Transparency International (TI) releasing its Corruption Perception Indices since 1998 has increasingly been showing that *Namibia is on the brink of being perceived as having significant problems with corruption. Since Namibia is still perceived to have significant problems with corruption, protracted effects are hard to ascertain in the short term on economic growth, private investment owing to higher costs and increasing uncertainty on the part of the investor, and price distortions.*

The Africa Competitiveness Report 2004 put Namibia on the seventh position on the public institutions and macroeconomic indices beaten by the likes of Malawi and Gambia. This also reflected the growing perception of increased levels of corruption and mismanagement at the parastatals and the local authorities.

I do not want to speculate on the sources and consequences of corruption at this stage. But evidences shows that rent seeking activities may be present in trade restrictions, low wage situation in public sector, natural resource endowments, and sociological factors. Consequences are hard to pin point at this stage. International evidence shows that corruption becomes more pervasive if there is too much government influence in the economy which is not growing. We do have greater government

influence but with moderate economic growth. Hence, moves aimed at ensuring regulation and establishment of institutions to counter corruption is timely at this stage so that it can reduce any opportunistic form of rent-seeking behavior and corruption.

*We may also follow the route of Botswana who has spent significant amounts on fighting corruption during the last decade, through investigating and prosecuting those found guilty, embarking on education campaigns against corruption and reviewing systems which may present opportunities for corruption. It is the only African country perceived not to have serious problems with corruption.*

In conclusion, allow me to end that despite putting in place regulations and establishment of appropriate institutions, it should be noted that officials in both private and public sectors who have discretion in applying rent seeking activities, would always do it and often willing to offer bribes and occasionally tempted to accept these bribes. The only way to ensure this does not happen is ensuring that it does not happen in the first place. Pay people well in those positions and ensure work ethic or culture that is counter corruptive but most importantly ensure punishment through legal recourse.

I thank you

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