

Governance

Overview

This report is about understanding and fixing government failures to provide the public goods needed for economic development. Governments play a unique role in economic development by providing the institutions that support competitive markets and by addressing those areas where markets fail. Governments also have unique powers for redistribution to complement other market-supporting policies to eradicate poverty and promote shared prosperity. Taken together, the government's role is paraphrased in the report as providing the public goods that it is uniquely positioned to provide. Governance is thus the process of pursuing policies to deliver public goods, using (and debating) the best available technical evidence for this purpose. Governments fail to provide public goods when leaders knowingly and deliberately ignore sound technical advice and adopt and implement policies that they know are costly, despite the availability of alternative policies that are likely to yield improved outcomes.¹

One example of government failure that has been widely studied and measured consists of malfeasance and mismanagement within public bureaucracies and by political leaders. Examples include: corruption; weak management practices that condone frequent absenteeism among public sector workers; nepotism in the recruitment and career advancement of public sector workers; and crony capitalism, whereby politically connected firms receive privileged treatment by public regulators.

Proximate factors behind widespread corruption in poor countries are the lower capacity of governments to monitor public officials, enforce rules, and design contracts that strengthen the economic incentives of

public officials to refrain from corruption. Significant evidence, however, suggests that systemic and persistent corruption has its roots in the actions of powerful leaders to extract rents from the state and deliberately weaken internal checks and balances. Even when leaders change and are replaced by well-intentioned reformers, the reformers can face the challenge of pervasive rent-seeking throughout the public sector that is suggestive of entrenched *norms of political behavior* to extract private benefits from public resources. Political norms are examined in this report as a subset of social norms, pertaining to the behavior of citizens and public officials specifically in the public sphere of governments. “Ordinary” citizens who hold no public office can be a part of government failure when they disregard the law and resort to bribery to avoid public interest regulations.

Corruption is not the only government failure. Even when government agencies are accountable for their actions, governance problems can originate from among citizens in the form of *what* they choose to demand and *for what* they hold government accountable. Citizens can be divided by ideological beliefs, leading to political polarization and policy gridlock. Ideological beliefs among citizens about specific public policies, such as energy subsidies or immigration, can be difficult to shift with technical evidence on the costs and benefits of different policy options. Similarly, distributive conflict among citizens, which leads special interest groups to mobilize to extract private benefits from public policies, frequently comes at the expense of the broader public interest.

Distributive conflict among, and inefficient demands from citizens, can lead to the selection of leaders who further polarize people and nurture ideological constituencies rather than exert effort to find common ground to address shared problems. These issues can also prevent reform leaders from pursuing appropriate public policies. Furthermore, this class of government failure is relevant for rich as well as for poor countries, and in weak as well as in stronger institutional environments, where internal checks and balances are more effective in controlling corruption in government.

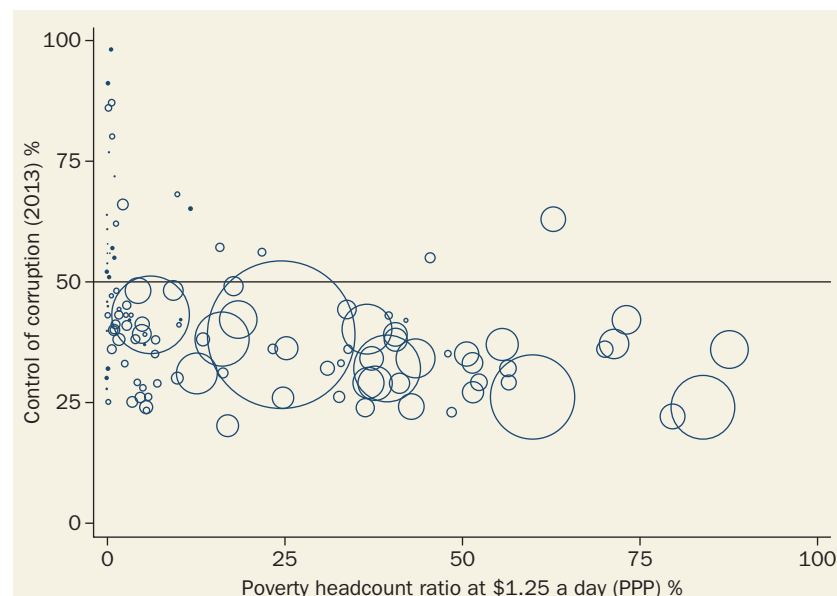
The next section of this chapter examines trends in corruption, one of the most widely studied government failures, and provides examples that show how persistent corruption can be rooted in adverse political incentives and perverse behavioral norms. The following section provides examples of how ideological beliefs and distributive conflict among citizens can be sources of government failures as well.

Trends in corruption

The vast majority of poor people live in countries with persistently low indicators of the control of corruption. A widely used measure in this regard is the Control of Corruption indicator of the World Bank's Worldwide Governance Indicators. The Control of Corruption measure "captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as 'capture' of the state by elites and private interests."² Figure 1.1 shows that nearly all of the world's poor people live in countries that are almost unanimously ranked in the bottom half of the indices of the control of corruption.

Not only is the control of corruption low in most developing countries, but it is persistently low. Figure 1.2 shows that most countries where poor people live have similar measures of corruption in 2013 as they did in 1996, the earliest and latest years for which these data are available.

Figure 1.1 Poor countries rank at the bottom on the control of corruption, 2013



Sources: Data on the Control of Corruption are from the Worldwide Governance Indicators (WGI) 2013. Data on the size of countries' poor population are from PovcalNet, an online tool for poverty measurement produced by the Development Research Group of the World Bank.

Note: Circles reflect size of countries' poor population. Y-axis measures a country's percentile ranking in Control of Corruption. X-axis measures the Poverty Headcount Ratio at \$1.25 a day (2005 PPP). PPP = purchasing power parity.

Figure 1.2 Persistence in corruption in poor countries, 2013 versus 1996



Sources: Data on the Control of Corruption are from the Worldwide Governance Indicators (WGI). Data on the size of countries' poor population are from PovcalNet (2005 PPP), an online tool for poverty measurement produced by the Development Research Group of the World Bank.
 Note: WGI data have been rescaled such that the lowest value of 0 (zero) corresponds to lowest control of corruption. The line represents the 45-degree line, where $y = x$. PPP = purchasing power parity.

Research on corruption has generally concluded that it has pernicious consequences for both the efficiency with which resources are allocated and for equity (Mauro 1995; Olken and Pande 2012). To highlight a few examples from this large literature, Fisman and Svensson (2007) find that bribes pose a greater cost to firms than an equivalent amount in taxes. Using firm-level data from Uganda, they find that the effect of an increase in bribery on reducing firm growth is three times greater than the impact of an equivalent amount of taxes. Meanwhile, Hunt (2007) shows that in Peru, victims of misfortune rely more on public services and, in turn, are more likely than nonvictims to need to bribe public officials. The poor do not spend a higher proportion of their income on bribes, but rather public services can fail them when they need it most and they can only access it through corruption.

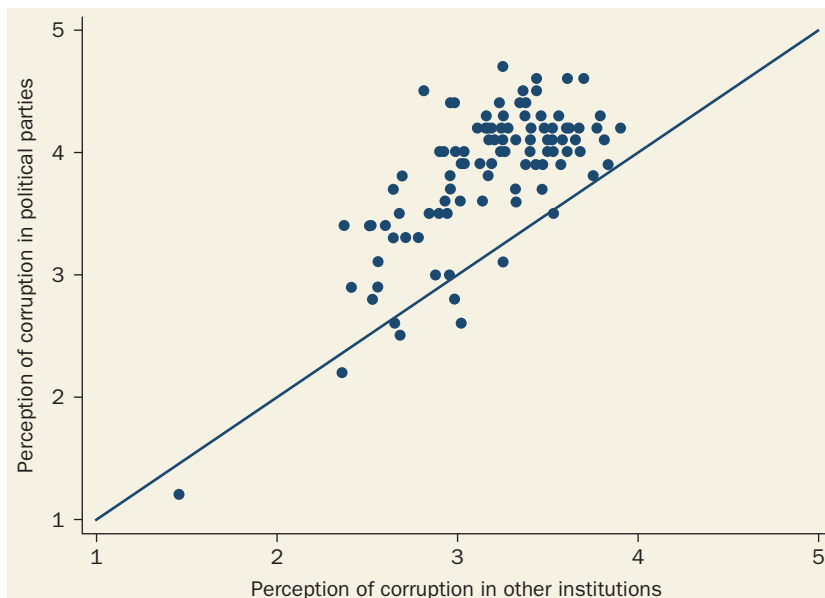
Corruption in politics

Systemic and persistent corruption has its roots in the actions of powerful leaders to deliberately weaken internal institutions of control within

government. A striking illustration of this comes from the detailed records of bribe payments to politicians, judges, and news media maintained by Vladimiro Montesinos, the head of Peru’s Intelligence Service under President Alberto Fujimori (McMillan and Zoido 2004). The average monthly amount of bribes going to politicians was US\$300,000, to judges US\$250,000, and to television channels US\$3 million. Bribes tended to be higher if the politician was part of the opposition and lower if the politician was from Fujimori’s party. The television channel with the largest viewership received US\$1.5 million monthly.

Transparency International’s Global Corruption Barometer (GCB) shows the extent of perceived corruption in politics. GCB is based on household surveys of more than 114,000 individuals. Patterns from the GCB in figures 1.3 and 1.4, below, reveal higher reports of corruption in political parties and the police, an instrument of the domestic coercive power of the state, compared with other institutions. The other institutions for which survey information was gathered include

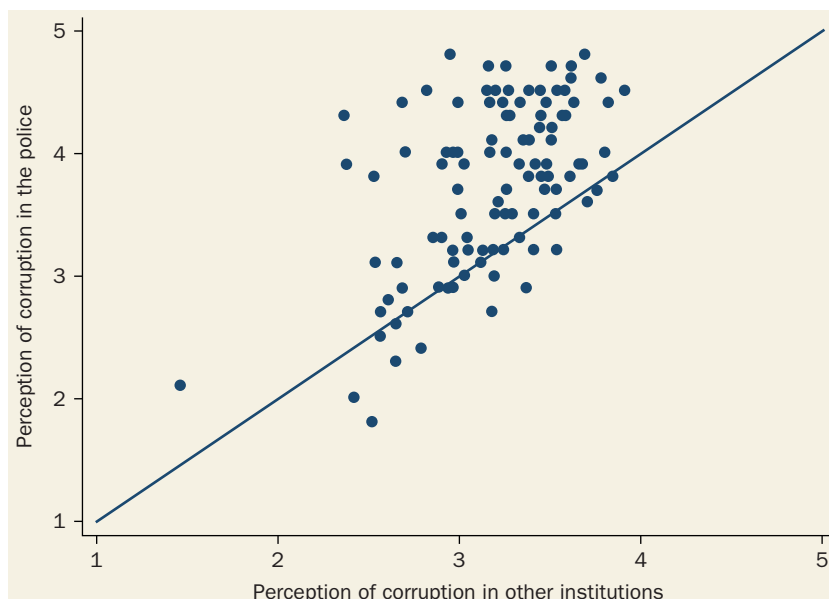
Figure 1.3 Perceived corruption in political parties versus in other institutions



Source: Global Corruption Barometer (GCB) 2013.

Note: GCB measures perceived corruption on a scale of 1–5, with 1 reflecting “not at all corrupt” and 5 reflecting “extremely corrupt.” The x-axis measures the average score of perceived corruption in the other institutions included in the GCB survey (other than political parties and the police), which are public officials/civil servants, judiciary, parliament/legislature, medical and health, education systems, military, nongovernmental organizations, media, religious bodies, and the business/private sector.

Figure 1.4 Perceived corruption in the police versus in other institutions



Source: Global Corruption Barometer (GCB) 2013.

Note: GCB measures perceived corruption on a scale of 1-5, with 1 reflecting “not at all corrupt” and 5 reflecting “extremely corrupt.” The x-axis measures the average score of perceived corruption in the other institutions included in the GCB survey (other than political parties and the police), which are public officials/civil servants, judiciary, parliament/legislature, medical and health, education systems, military, nongovernmental organizations, media, religious bodies, and the business/private sector.

public officials/civil servants, parliament/legislature, judiciary, military, nongovernmental organizations (NGOs), the media, religious bodies, business/private sector, education system, and medical/health. The results, therefore, show that citizens systematically report greater corruption in political parties and the police than in other institutions. They suggest that corruption pervades the institutions through which leaders gain public office and wield power within government.

Political connections and corruption

Research provides evidence that political connections are used by economic agents to gain an advantage over competitors in countries with weak control of corruption. Faccio (2006) examines 20,202 publicly traded firms in 47 countries and finds that politically connected firms are more common in countries with high corruption. Moreover, political connections are significantly associated with a higher share value of firms in countries with

high corruption: having a member of a firm's board or a large shareholder become a politician is associated with an increase in the firm's stock value of 4.43 percent. In contrast, there is no significant association of firm value with political connections in countries with low corruption.

These cross-country findings are bolstered by within-country research. In Indonesia, Fisman (2001) finds that the value of firms depends on the degree of their political connectedness. Following rumors of President Suharto's worsening health during 1995–97, the stock price of politically connected firms fell more than that of less connected firms. Another contrast, similar to the results in Faccio (2006) of political connections in weak versus strong institutional environments comes from Fisman et al.'s (2012) replication of the methodology used in Indonesia to estimate the value of political connections in the United States to former U.S. Vice President Dick Cheney. In contrast to political connections to President Suharto, they find no effect of connections to Vice President Cheney. Companies with personal connections to Vice President Cheney are unaffected by events that would be expected to affect Vice President Cheney's capacity to give companies preferential treatment. The authors conclude that strong institutions in the United States are effective in reining in rent-seeking through connections to high-level politicians.

Meanwhile, in Pakistan, Khwaja and Mian (2005) consider data on firms' borrowing from banks between 1996 and 2002, and find that politically connected firms, defined as those having a politician on the firm's board, borrow 45 percent more and have a 50 percent higher default rate. The effects are greater depending on whether the political party to which the firm is connected is in power. Rijkers, Freund, and Nucifora (2014) provide evidence from firm-level data in Tunisia that suggests that Tunisia's industrial policy was used as a vehicle for rent creation for President Ben Ali and his family. Diwan, Keefer, and Schiffbauer (2015) provide evidence from the Arab Republic of Egypt that entry by politically connected firms slows aggregate employment growth and skews the distribution of employment toward less productive, smaller firms.

Connections are also important at the local level. Political connections to local leaders are associated with greater absenteeism among frontline public service providers and lower motivation on the job. Callen et al. (2014) provide systematic evidence that politically connected doctors in Pakistan are more likely to be absent from public health clinics. They also find that about 40 percent of inspectors and health administrators report political interference when they try to sanction errant doctors.

La Forgia et al. (2014) provide case studies from India of a thriving “parallel system” for human resources management in the public health sector that is based on political connections and bribes, rather than on formal rules. Through connections and bribes, doctors are able to obtain the public clinic posts they desire, regardless of their performance on the job. Linking this study to another by Das et al. (2015) on the performance of public sector doctors in India suggests that this parallel system results in rampant underperformance. Das et al. (2015) show that doctors in the public sector in India perform significantly worse, not only compared with their counterparts in the private sector, but also when they provide services through public clinics rather than in their private practices. Furthermore, although provider effort and prices charged in the private sector are strongly and positively correlated, there is no correlation between effort and wages in the public sector.

Detailed case studies suggest that in environments with widespread rent-seeking, all types of officials in the public sector, ranging from the humble administrator and local political leader at the street level (Lipsky 1980) up to powerful politicians at the regional or national levels, can gear their discretion, ingenuity, and entrepreneurship toward finding ways to circumvent internal controls rather than solving problems in the public interest.

The point is illustrated in a quote provided by Zimmerman (2014), which is attributed to an official in the Anti-Corruption Bureau in Malawi who is discussing local corruption in the implementation of national programs:

In the early years of the fertilizer subsidy programme, politicians would take the fertilizer bags at distributions in the presence of the people. This was discovered and there was outrage, so then fertilizer started to go missing on the journey to distributions. This was discovered and there was more outrage, so then beneficiaries who did not exist received fertilizer for a time, until this was also discovered and there was more outrage once again. Lately, the fertilizer is distributed to real beneficiaries during real distributions, but in advance the bags of fertilizer have been opened and diluted with sand. Some officials, seeing the anger over the subsidy program, have stopped their corruption there and have begun corruption in areas that do not anger the people, such as manipulating district bank accounts.

In India, Aiyar and Mehta (2015) provide examples of how local political leaders circumvent internal controls in India's flagship antipoverty program, established by the Mahatma Gandhi National Rural Employment Guarantee Act. The authors study the functioning of social audits in India, a recent institutional arrangement aimed at checking local rent-seeking by engaging citizens to directly monitor public spending. Their field work was conducted in Andhra Pradesh, a state that has been lauded for systematically investing in social audits. Aiyar and Mehta (2015) provide examples of politicians extracting large rents from this antipoverty scheme by circumventing the social audit altogether. Connections between local political elites are forged and maintained for the purpose of big-ticket theft from state funds that social audits cannot uncover.

Culture of corruption

Other evidence shows just how widespread is the practice of bribing public officials and, in that sense, the norm of behavior in the public sector in environments with high corruption. Bribe payments to public officials occur in all manner of transactions in which citizens interact with the state in poor countries, either as users of services or as owners and employers of businesses. Such interactions follow the economic dynamics of competitive markets for bribery. In a detailed empirical study of bribes paid by truck drivers in Indonesia to police and military officials to avoid harassment at checkpoints and to weigh station attendants to avoid fines for driving overweight, Olken and Barron (2009) find that the demand for illegal payments by officials adheres to standard economic models of pricing behavior.

Similarly, another study in Indonesia by Burgess et al. (2012) on the incentives of local public officials and politicians to enforce forest policy and prevent illegal logging finds evidence consistent with economic models of how officials will behave to allow deforestation, presumably in exchange for bribes. When a province is subdivided and a new district is created, greater competition among the newly created jurisdictions drives down the price for wood and increases the overall rate of deforestation in the province. Illegal logging also increases substantially in the years leading up to local elections. In a similar vein, Fan, Lin, and Treisman (2009) find that firms' reports of bribe payments to public officials are more frequent in countries with more administrative tiers of government.

The above evidence (such as in Olken and Barron [2009]) shows that the behavior of public officials is sensitive to incentives, such that there

is little reason to believe in a “culture of corruption” that is rooted in mindsets and mental models that are impervious to rational incentives and hard to change. The evidence is also consistent with another view of a culture of corruption that stems from rational beliefs about how others are behaving and about the probability of detection and punishment in environments with widespread corruption and scarce resources to combat it. This analysis follows one element in the definition of “culture” in Alesina and Giuliano (forthcoming) and Greif (1994) as beliefs about the consequences of one’s actions that are based on expectations of actions others will take.³ This view suggests that a culture of corruption may not be as slow to change as other aspects of cultural beliefs and values, such as those derived from religion or inherited social norms. Instead, it may be more sensitive to experience and information in updating beliefs.

Fisman and Miguel (2007) provide evidence that both cultural norms and short-term changes in incentives in response to legal enforcement are important determinants of corrupt behavior. They find that foreign diplomats posted in New York City who come from countries with higher measures of corruption accumulated significantly more unpaid parking violations compared with their peers from better-governed countries. This finding suggests that the elite from countries with more widespread corruption have a greater proclivity to corruption than other elites in the same situation. However, they also find that the apparent norm of corruption among foreign diplomats was quickly overcome when the laws were changed to allow parking enforcement authorities to confiscate the diplomatic license plates of violators.

The quick and large impact of a change in enforcement laws observed by Fisman and Miguel (2007) was presumably facilitated by already-functioning, strong institutions of enforcement in New York City. The challenge for countries with weak institutions, and low capacity and resources for monitoring and enforcement to begin with, is how to leverage these scarce resources to tackle widespread corruption.

If prevailing incentives shape corruption, then policy initiatives can be designed to reshape those incentives to combat corruption. However, when corruption is the norm, efforts to control it through different approaches to monitoring and enforcement can be more challenging than when corruption is an aberration. Lui (1986) develops a multiple equilibrium model showing that when corruption is widespread, it is costly to reduce and difficult to detect and so the economy will remain highly corrupt. Tirole (1996)

models how corruption may persist over generations. He models individual reputations as the aggregate of collective reputations and individuals' current incentives as shaped by the behavior of previous generations. The persistence of corruption among bureaucrats, for example, might reflect a corrupt reputation of previous generations and the lack of incentives to act honestly if enough bureaucrats are corrupt.⁴

Other evidence suggests that individuals with a higher proclivity to corruption might self-select into the public sector for rent-seeking motives. Hanna and Wang (2013) show that students in India who cheat on a simple task in a lab experiment are more likely to have a preference for public sector jobs. They also find that cheating on the task predicts actual corruption by government officials, consistent with the task capturing a meaningful predilection for corruption. Selection of individuals into the public sector for rent-seeking motives, or turning to corruption while in office because of the incentives and the perceived behavioral norms among colleagues, can lead to the persistence of corruption.

Citizens' attitudes to corruption

Behavioral norms to extract private benefits from public resources extend to "ordinary" citizens who hold no public office. The examples from the research discussed above not only show widespread demand for bribes among public officials but also that citizens supply bribes precisely for the purpose of deriving private rents at the expense of the greater public interest. Overweight trucks, as in the study by Olken and Barron (2009), damage public infrastructure, but truck drivers have incentives to bribe weigh station attendants to avoid regulations on weight. Greater deforestation has been associated with environmental and health problems (for example, Garg 2014), but owners of logging companies bribe local officials to get away with illegal logging (Burgess et al. 2012).

"Free-riding" among citizens can lead to lower contributions to the public good of monitoring and sanctioning public officials who engage in corruption. Few people are likely to take the costly actions needed to monitor and sanction public officials, or to desist from colluding with rent-seeking officials (as in the examples of overweight trucks and illegal deforestation), especially when they believe that others are unlikely to join them. As evidence of the free-riding problem, research has found a significant difference in citizen monitoring of different types of corruption depending on whether the monitoring would yield immediate private

benefits versus more broadly shared benefits. Olken (2007) finds that community members in Indonesia are more likely to monitor and demand accurate wage payments from local officials who manage workfare projects, the benefits from which they receive individually. In contrast, community members are less likely to engage in local collective action along with others to reduce leakage in project materials costs whose benefits would accrue to the whole community.

Similarly, free-riding problems among citizens in monitoring and sanctioning public providers—for example, school teachers in India—appears in the research of Banerjee et al. (2010). The authors find that, in response to an information campaign about the poor quality of education provided in the village public schools, community members were willing to undertake private action, such as remedial instruction for their own children outside school, but not to take collective action to improve the performance of the village public school.

Citizens' behavior toward the public sector can contribute to government failures. One example is the widespread theft of electricity from public utilities, which leads to disruptions in electricity supply that cripple economic investments (Depuru, Wang, and Devabhaktuni 2011). Citizens describe such theft from the public sector in particular as justifiable, even though theft in general is considered wrong. Evidence of political leaders manipulating the electricity supply to facilitate an increase in theft at election times suggests that citizen behavior toward the state is influenced by politics (Min 2015; Min and Golden 2014). Corruption and poor service delivery can diminish the legitimacy of the state and lead citizens to organize for violent conflict (World Bank 2011). Such disregard for state institutions and laws reflects weak norms for cooperative behavior in the public sphere, which can keep societies trapped in a situation of persistent corruption and weak institutions (Basu 2015; P. Dal Bó 2007).

Government failures arising from beliefs about how others are behaving, rather than because of an inherited mindset or cultural values, can also change rapidly when people see changes in how others are behaving. A quote from an Egyptian student reflecting on people cleaning up Tahrir Square illustrates this: “We thought people didn’t care and just threw their garbage on the street, but now we see that they just thought it was hopeless—why bother when it’s so dirty. Why not be corrupt when everything is corrupted. But now things have changed, and it’s a different mood overtaking. Even I can’t stop smiling myself.” (Steavenson 2011, 45).

Ideological beliefs and distributive conflict among citizens

Political impediments to selecting and implementing technically sound policies can arise even when governments are accountable to citizens and corruption is rare. Citizens' beliefs about public policies and demands for specific policies without full regard for the costs they may entail can hamper the selection of public policies on the basis of technical merit.

Different strands of research provide evidence on three channels. First, ideological beliefs about appropriate public policies can be resistant to technical evidence that is contrary to those prior beliefs. Second, lack of information or limited cognitive capacity to process information about the consequences of different policies can also lead to demand for inefficient policies. Third, special interests and distributive conflict among different groups of citizens can distort policies to benefit those who organize to pursue their interests at the expense of the greater public good. Some leaders can exploit these political beliefs and special interests to gain and remain in office by dividing citizens and polarizing constituencies rather than building common cause for public goods.

One policy area that serves to illustrate these points is that of energy or fuel subsidies. Technical evidence and wide agreement among experts indicates that fuel subsidies are inefficient and entail fiscal and environmental costs with little justification on equity grounds (Clements et al. 2013). Fuel subsidies in the developing world are highly regressive (Arze del Granado, Coady, and Gillingham 2012). In India, estimates suggest that the richest 10 percent of households receive seven times more in benefits from subsidies than the poorest 10 percent (Anand et al. 2013). A common view of the regressive incidence of energy subsidies is that costly fuel subsidies are a form of elite capture. A typical strategy used to win political support for reforms is to replace energy subsidies with cash transfers to the poor.⁵ The underlying rationale is that, if people realize that the lion's share of subsidies accrues to the elite, they will punish political leaders who allocate public resources to these subsidies and reward them for allocating means-tested cash transfers to the poor.

However, if subsidies are popular because of ideological beliefs that they are "pro-poor," that governments *should* pursue price controls in addition to providing cash transfers to the poor, then even seeming reforms that curtail some subsidies may be transient and ineffective. When a price shock hits, people will be out on the streets again asking for subsidies or an

increase in the cash transfer to compensate for the price increase (Clements et al. 2013). Little evidence is available to determine whether costly subsidy policies are sustained due to capture by elites or organized special interests, due to informational and cognitive constraints among citizens to recognize the costs of these policies or due to ideological beliefs about the value of such policies. However, some evidence from the United States on citizen attitudes toward combating climate change with energy policies suggests that the latter two explanations are likely to be a significant part of the story for why it is difficult to reform energy subsidies.

Dal Bó, Dal Bó, and Eyster (2013) and Sunstein (2007) provide evidence from laboratory experiments in the United States suggesting that citizens are cognitively constrained to demand policies that confer short-term benefits at the expense of long-term or “equilibrium” costs. That is, citizens fail to internalize the full impact of the demand for a particular policy.

A related but different argument is proposed by Kahan (2012) and Kahan, Jenkins-Smith, and Braman (2011). Also using laboratory experiments in the United States, these authors show that those who score highest on cognitive abilities are also the most likely to adopt ideological beliefs in defiance of technical evidence. The authors explain this as “motivated reasoning” that is adopted by people to conform to the values of the cultural groups to which they belong. Their findings suggest that public divisions over climate change are not a reflection of the public’s lack of knowledge or misunderstanding of science; rather, divisions stem from conflicting interests—between an individual’s interests in adopting common beliefs held by one’s community versus a collective interest in making decisions to promote common welfare. Holding a viewpoint that goes against one’s surrounding cultural community can exact a cost. When this cost is high, it is rational for individuals to adopt the reasoning prevailing in the group.

Together, this work substantiates the role of beliefs and behavioral norms in shaping citizens’ demands for public policies. They differ in their view of the extent to which citizens’ resistance to technical evidence is caused by cognitive constraints. Kahan (2012) and Kahan, Jenkins-Smith, and Braman (2011) highlight the importance of cultural norms instead of cognitive constraints, arguing that citizens engage in motivated reasoning to conform an assessment of available facts to the beliefs of the social groups to which they belong.

This research from the United States on citizens’ beliefs and attitudes toward public policies suggests that rigorous scientific methods need to be

applied to develop an understanding of the sources of political impediments rather than assuming a “common sense” understanding of it. It also has implications for communicating technical evidence to people, highlighting the issues of social and ideological divisions and resistance to such evidence even among educated citizens. Scientific rigor is also needed to understand how communication can be persuasive and shift beliefs. That is, simply providing information assuming that it will address an information asymmetry will not work if the problem is rooted in beliefs and behavioral norms. The following chapters of this report are aimed at reviewing available research on how transparency and political engagement, and the leaders selected through it, play a role in shifting beliefs.

In addition to holding ideological beliefs and the existence of cognitive capacity constraints, special interest groups and elite capture are the third channel through which citizens’ behavior poses political impediments to the adoption of sound public policies. The theory and evidence on special interest groups shows how citizens can organize to distort policies away from the broad public interest and toward conferring narrow benefits to group members (Grossman and Helpman 2001). This work focuses on environments with strong institutional constraints such as in the United States, showing that political impediments can arise from among citizens even when accountability institutions function well. Gilens and Page (2014) provide evidence to suggest that economic elites and organized groups representing business interests substantially influence U.S. government policy. In their seminal work in the developing world, Bardhan and Mookherjee (2000) model elite capture similarly to the modeling of special interests in the U.S. literature.

A related strand of research provides evidence on how ideological commitment to political parties can yield policy gridlock due to political polarization in rich countries (Glaeser and Sunstein 2013). Although well-functioning political parties, organized around policy programs, can solve some collective action problems (Keefer and Vlaicu 2007), they can contribute to other problems that arise from the ideological preferences of voters. In addition to policy gridlock in advanced institutional contexts, partisan preferences can facilitate corruption and rent-seeking in weak institutional environments (Bardhan and Mookherjee 2010).

Bardhan and Mookherjee (2010) find evidence suggesting that political parties can use partisan attachment among voters to pursue rents and reduce effort rather than to deliver the policies that their party espouses. The authors use data on a sample of villages spanning 1974–98 to

investigate the political determinants of land reform implementation in the Indian state of West Bengal. A relatively well-organized and programmatic party used to dominate the political arena in West Bengal during this period—the Communist Party of India (Marxist) with a strong political commitment to land reform. The authors find that the relationship between the party’s control of local governments and implementation of land reform is consistent with both reelection concerns and rent-seeking. Villages with more closely contested elections experience more land reform. However, once the party gains a majority, land reform decreases despite the party’s commitment to it.

Redistributive conflict among groups of citizens who are divided along different cleavages, such as ethnic identity, is a related source of impediments to policies for public goods. Ethnic divisions are regarded by some scholars as central to the explanation of why some regions of the world are rich and others are persistently poor (Ashraf and Galor 2013). Substantial evidence exists of an association between ethnic fragmentation and low investment in public goods (Habyarimana et al. 2009; Miguel and Gugerty 2005).

Alesina, Michalopoulos, and Papaioannou (forthcoming) find that it is not ethnic fragmentation per se that matters in explaining variations in economic development, but rather its interaction with economic inequality. Economic inequality between ethnic groups, largely arising from differences in geographic endowments across their historic homelands, is associated with lower real gross domestic product (GDP) per capita. The typical measure of ethno-linguistic fragmentation used in the literature loses its significance when the authors’ measure of economic inequality between ethnic groups is included. This result is consistent with the view that redistributive conflict between groups can contribute to political failures to select and implement appropriate public policies that promote economic development.

Banerjee and Pande (2007) provide micro evidence in support of the hypothesis that redistributive conflict among citizens contributes to leaders’ weak political incentives to provide public goods. They document that, in the state of Uttar Pradesh in India, political parties are organized to appeal to caste identity and regularly field candidates against whom there are allegations of corruption and criminality. The authors explain this through a model in which greater corruption arises in ethnic parties because citizens value honesty in political leaders less than reliable redistribution based on shared ethnic identity. At the same time, in other work

these authors show that voter preferences regarding ethnic identity are malleable and responsive to information about the severity of allegations of transgression (Banerjee et al. 2009; Banerjee et al. 2014).

As the evidence grows on both ethnic politics in the developing world and ideological politics in the rich world, it appears that both types of divisions play a similar role of stoking conflict among citizens over the distribution of public resources, which undermines the use of these resources in addressing shared problems of public goods.

This chapter has set the stage by describing government failures that affect countries around the world and the need to solve these so that public sector institutions are capable of tackling problems of public goods. Incentives and behavioral norms among political leaders, public officials, frontline public service providers, and citizens alike can contribute to government failure. Persistent and widespread corruption in developing countries is consistent with a culture of corruption based on rational beliefs about how others are behaving in the public sector. Corruption is not the only government failure. Ideological beliefs about public policies and distributive conflict among citizens over the allocation of public resources also contribute to government failure. These problems are shared by rich and poor countries, and those with strong and weak institutions to control malfeasance and mismanagement within government.

The objective of the report is to examine how these government failures can be overcome by harnessing two forces that are spreading around the world: citizen engagement and transparency in political processes. The next two chapters examine these trends.

Notes

1. Governments can make inadvertent mistakes when they do not have the right evidence or when the state of the world changes and they need to find out what to do to tackle new problems as they emerge. Such mistakes, uncertainties, or technical debates about appropriate public policies are not part of how government failure is defined in this report. Government failure is defined on the basis of purpose, intent, and incentives of leaders to not pursue public policies in the public interest. In chapter 4, the conceptual framework of the report reviews the economic theory supporting this view of government failure.
2. Worldwide Governance Indicators, <http://info.worldbank.org/governance/wgi/pdf/cc.pdf>.

3. Alesina and Giuliano (forthcoming) discuss how this definition of culture overlaps with what others have described as “informal institutions.” They also discuss the links between the view of culture as a set of rational beliefs with the view of “mental constructs” that generate different beliefs and can persist over time (Benabou 2008).
4. The evidence shows that even in environments with widespread corruption, when policy initiatives provide credible incentives, monitoring, and enforcement, corruption is reduced (for example, Di Tella and Schargrodsky [2003]; Muralidharan, Niehaus, and Sukhtankar [2014]). The discussion in this section is not intended to underestimate the role of technologies that reduce opportunities for corruption or of investments in monitoring and enforcement. It is aimed at including the concepts of how beliefs and behavioral norms might matter as well. This discussion is important for exploring how other policy areas aimed at strengthening political incentives and changing political beliefs and behavioral norms can complement technological solutions to governance problems and increase the likelihood of take-up.
5. An example is provided by the exchange around the following blog post: <http://blogs.worldbank.org/futuredevelopment/lessons-reducing-energy-subsidies>.

Bibliography

- Aiyar, Yamini, and Soumya Kapoor Mehta. 2015. “Spectators or Participants? Effects of Social Audits in Andhra Pradesh.” *Economic and Political Weekly* 50 (7): 66–71.
- Alesina, Alberto, and Paola Giuliano. Forthcoming. “Culture and Institutions.” *Journal of Economic Literature*.
- Alesina, Alberto, Stelios Michalopoulos, and Elias Papaioannou. Forthcoming. “Ethnic Inequality.” *Journal of Political Economy*.
- Anand, Rahul, David Coady, Adil Mohommad, Vimal Thakoor, and James P. Walsh. 2013. “The Fiscal and Welfare Impacts of Reforming Fuel Subsidies in India.” IMF Working Paper 13/128. International Monetary Fund, Washington, DC.
- Arze del Granado, J., D. Coady, and R. Gillingham. 2012. “The Unequal Benefits of Fuel Subsidies: A Review of Evidence for Developing Countries.” *World Development* 40 (11): 2234–48.
- Ashraf, Q., and O. Galor. 2013. “The Out of Africa Hypothesis, Human Genetic Diversity and Comparative Economic Development.” *American Economic Review* 102 (1): 1–46.
- Banerjee, Abhijit V., Rukmini Banerji, Esther Duflo, Rachel Glennerster, and Stuti Khemani. 2010. “Pitfalls of Participatory Programs: Evidence from a Randomized Evaluation in Education in India.” *American Economic Journal: Economic Policy* 2 (1): 1–30.
- Banerjee, Abhijit, Donald Green, Jennifer Green, and Rohini Pande. 2009. “Can Voters Be Primed to Choose Better Legislators? Evidence from Two Field Experiments in Rural India.” Unpublished.

- Banerjee, Abhijit, Donald P. Green, Jeffery McManus, and Rohini Pande. 2014. "Are Poor Voters Indifferent to Whether Elected Leaders Are Criminal or Corrupt? A Vignette Experiment in Rural India." *Political Communication* 31 (3): 391–407.
- Banerjee, Abhijit, and Rohini Pande. 2007. "Parochial Politics: Ethnic Preferences and Politician Corruption." Working Paper, Kennedy School of Government, Harvard University, Cambridge, MA.
- Bardhan, Pranab, and Dilip Mookherjee. 2000. "Capture and Governance at Local and National Levels." *American Economic Review* 90 (2): 135–39.
- . 2010. "Determinants of Redistributive Politics: An Empirical Analysis of Land Reforms in West Bengal, India." *American Economic Review* 100 (4): 1572–600.
- Basu, K. 2015. *The Republic of Beliefs: A New Approach to Law and Economics*. Washington, DC: World Bank.
- Benabou, R. 2008. "Ideology." *Journal of the European Economic Association* 6 (2–3): 321–52.
- Burgess, Robin, Benjamin Olken, Matthew Hansen, Peter Potapov, and Stefanie Sieber. 2012. "The Political Economy of Deforestation in the Tropics." *Quarterly Journal of Economics* 127 (4): 1707–54.
- Callen, Michael, Saad Gulzar, Ali Hasanain, and Yasir Khan. 2014. "The Political Economy of Public Employee Absence: Experimental Evidence from Pakistan: Do Local Politics Determine the Effectiveness of Development Interventions? Why Are Service Providers Commonly Absent in Developing Countries?" Unpublished, Harvard Kennedy School.
- Clements, Benedict J., David Coady, Stefania Fabrizio, Sanjeev Gupta, Trevor Alleyne, and Carlo Sdravovich, eds. 2013. *Energy Subsidy Reform: Lessons and Implications*. Washington, DC: International Monetary Fund.
- Dal Bó, Ernesto. 2007. "Bribing Voters." *American Journal of Political Science* 51(4): 789–803.
- Dal Bó, Ernesto, Pedro Dal Bó, and Erik Eyster. 2013. "The Demand for Bad Policy When Voters Underappreciate Equilibrium Effects." Unpublished working paper. http://faculty.haas.berkeley.edu/dalbo/demand_for_bad_policy.pdf.
- Dal Bó, Pedro. 2007. "Social Norms, Cooperation and Inequality." *Economic Theory* 30 (1): 89–105.
- Das, Jishnu, Alaka Holla, Aakash Mohpal, and Karthik Muralidharan. 2015. "Quality and Accountability in Healthcare Delivery: Audit Evidence from Primary Care Providers in India." Policy Research Working Paper No. WPS 7334, World Bank, Washington, DC.
- Depuru, Soma Shekara Sreenadh Reddy, Lingfeng Wang, and Vijay Devabhaktuni. 2011. "Electricity Theft: Overview, Issues, Prevention and a Smart Meter Based Approach to Control Theft." *Energy Policy* 39 (2): 1007–15.
- Di Tella, R., and E. Schargrodsy. 2003. "The Role of Wages and Auditing during a Crackdown on Corruption in the City of Buenos Aires." *Journal of Law and Economics* 46 (1): 269–92.
- Diwan, Ishac, Philip Keefer, and Marc Schiffbauer. 2015. "Pyramid Capitalism: Political Connections, Regulation, and Firm Productivity in Egypt." World Bank Policy Research Working Paper 7354, World Bank, Washington, DC.

- Faccio, Mara. 2006. "Politically Connected Firms." *American Economic Review* 96 (1): 369–86.
- Fan, C. Simon, Chen Lin, and Daniel Treisman. 2009. "Political Decentralization and Corruption: Evidence from around the World." *Journal of Public Economics* 93 (1–2): 14–34.
- Fisman, David, Raymond J. Fisman, Julia Galef, Rakesh Khurana, and Yongxiang Wang. 2012. "Estimating the Value of Connections to Vice-President Cheney." *BE Journal of Economic Analysis and Policy* 13 (3): 1–20.
- Fisman, Raymond. 2001. "Estimating the Value of Political Connections." *American Economic Review* 91(4): 1095–102.
- Fisman, Raymond, and Edward Miguel. 2007. "Corruption, Norms, and Legal Enforcement: Evidence from Diplomatic Parking Tickets." *Journal of Political Economy* 115 (6): 1020–48.
- Fisman, Raymond, and Jakob Svensson. 2007. "Are Corruption and Taxation Really Harmful to Growth? Firm Level Evidence." *Journal of Development Economics* 83 (1): 63–75.
- Garg, Teevrat. 2014. "Public Health Effects of Natural Resource Degradation: Evidence from Deforestation in Indonesia." Job Market Paper, Cornell University, Ithaca, NY.
- Gilens, Martin, and Benjamin I. Page. 2014. "Testing Theories of American Politics: Elites, Interest Groups, and Average Citizens." *Perspectives on Politics* 12 (3): 564–81.
- Glaeser, Edward, and Cass Sunstein. 2013. "Why Does Balanced News Produce Unbalanced Views?" NBER Working Paper 18975, National Bureau of Economic Research, Cambridge, MA.
- Greif, Avner. 1994. "Cultural Beliefs and the Organization of Society: A Historical and Theoretical Reflection on Collectivist and Individualist Societies." *Journal of Political Economy* 102 (5): 912–50.
- Grossman, Gene M., and Elhanan Helpman. 2001. *Special Interest Politics*. Cambridge and London: MIT Press.
- Habyarimana, James, Macartan Humphreys, Daniel Posner, and Jeremy Weinstein. 2009. *Coethnicity: Diversity and the Dilemmas of Collective Action*. New York: Russell Sage Foundation.
- Hanna, Rema, and Shing-Yi Wang. 2013. "Dishonesty and Selection into Public Service: Evidence from India." NBER Working Paper 19649, National Bureau of Economic Research, Cambridge, MA.
- Hunt, Jennifer. 2007. "How Corruption Hits People when They Are Down." *Journal of Development Economics* 84 (2): 574–89.
- Kahan, Dan M. 2012. "Ideology, Motivated Reasoning, and Cognitive Reflection: An Experimental Study." *Judgment and Decision Making* 8 (4): 407–24.
- Kahan, Dan M., Hank Jenkins-Smith, and Donald Braman. 2011. "Cultural Cognition of Scientific Consensus." *Journal of Risk Research* 14 (2): 147–74.
- Keefer, Philip, and Razvan Vlaicu. 2007. "Democracy, Credibility and Clientelism." *Journal of Law, Economics and Organization* 24 (2): 371–406.
- Khwaja, Asim Ijaz, and Atif Mian. 2005. "Do Lenders Favor Politically Connected Firms? Rent Provision in an Emerging Financial Market." *Quarterly Journal of Economics* 120 (4): 1371–411.

- La Forgia, Gerard M., Shomikho Raha, Shabbeer Shaik, Sunil Kumar Maheshwari, and Rabia Ali. 2014. "Parallel Systems and Human Resource Management in India's Public Health Services: A View from the Front Lines." Policy Research Working Paper No. 6953, World Bank, Washington, DC.
- Lipsky, Michael. 1980. *Street-Level Bureaucracy: Dilemmas of the Individual in Public Services*. New York: Russell Sage Foundation.
- Lui, Francis. 1986. "A Dynamic Model of Corruption Deterrence." *Journal of Public Economics* 31 (2): 215–36.
- Mauro, Paolo. 1995. "Corruption and Growth." *Quarterly Journal of Economics* 110 (3): 681–712.
- McMillan, John, and Pablo Zoido. 2004. "How to Subvert Democracy: Montesinos in Peru." *Journal of Economic Perspectives* 18 (4): 69–92.
- Miguel, E., and M. K. Gugerty. 2005. "Ethnic Diversity, Social Sanctions, and Public Goods in Kenya." *Journal of Public Economics* 89 (11): 2325–68.
- Min, Brian. 2015. *Power and the Vote: Elections and Electricity in the Developing World*. New York: Cambridge University Press.
- Min, Brian, and Miriam Golden. 2014. "Electoral Cycles in Electricity Losses in India." *Energy Policy* 65: 619–25.
- Muralidharan, Karthik, Paul Niehaus, and Sandip Sukhtankar. 2014. "Building State Capacity: Evidence from Biometric Smartcards in India." NBER Working Paper 19999, National Bureau of Economic Research, Cambridge, MA.
- Olken, Benjamin. 2007. "Monitoring Corruption: Evidence from a Field Experiment in Indonesia." *Journal of Political Economy* 115 (2): 200–49.
- Olken, Benjamin, and Patrick Barron. 2009. "The Simple Economics of Extortion: Evidence from Trucking in Aceh." *Journal of Political Economy* 117 (3): 417–52.
- Olken, Benjamin A., and Rohini Pande. 2012. "Corruption in Developing Countries." *Annual Review of Economics* 4 (1): 479–509.
- Rijkers, Bob, Caroline Freund, and Antonio Nucifora. 2014. "All in the Family: State Capture in Tunisia." World Bank Policy Research Working Paper 6810, World Bank, Washington, DC.
- Stevenson, Wendell. 2011. "Letter from Cairo: On the Square—Between the Protesters and the Military." *New Yorker*, February 28, 36–45.
- Sunstein, Cass. 2007. "On the Divergent American Reactions to Terrorism and Climate Change." *Columbia Law Review* 107 (2): 503–57.
- Tirole, Jean. 1996. "A Theory of Collective Reputations (with Applications to the Persistence of Corruption and to Firm Quality)." *Review of Economic Studies* 63 (1): 1–22.
- World Bank. 2011. *World Development Report 2011: Conflict, Security, and Development*. Washington, DC: World Bank. <https://openknowledge.worldbank.org/handle/10986/4389>.
- Zimmerman, Brigitte. 2014. "Transparency, Sanctioning Capacity, and Corruption Displacement: Multi-Method Evidence from Local Government in Malawi." PhD Dissertation, University of California San Diego.