Corporate Governance and Corruption: A Cross-Country Analysis

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Because the empirical literature on the causes of corruption has focused primarily on the demand side of corruption, that is, the corrupt officials who receive bribe payments, the role of the private sector as the supply side of corruption has not been examined thoroughly in this literature. In this article, it is argued that corporate governance is among the important factors determining the level of corruption. Using a cross-country data set, hypotheses that explicitly link various measures of corporate governance to the level of corruption are tested. The results show that corporate governance standards can have profound impacts on the effectiveness of the global anticorruption campaign.

INTRODUCTION

Corporate governance has emerged as a major policy concern for many developing countries following the financial crisis in Asia, Russia, and Latin America. The collapse of Enron suggests that even the highly industrialized countries such as the U.S. are not immune to the disastrous effects of bad corporate governance. Studies have shown that low corporate governance standards raise the cost of capital, lower the operating performance of industry, and impede the flow of investment (Agrawal and Knoeber; Daily and Dalton; Himmelberg, Hubbard, and Love). Following the corporate scandals of Enron, WorldCom, and Tyco, more and more countries have embarked on corporate governance reforms to better protect the interests of investors.

Policy makers around the world have another important reason to be concerned with corporate governance: poor corporate governance also breeds corruption. Corruption, defined here as the misuse of public office for private gain (Rose-Ackerman 1978), has both demand and supply sides to it. While much attention to the global anticorruption campaign has been directed toward the demand side of corruption (Vogl), that is, the corrupt government officials, the supply side of corruption is just as important, and the role of the corporations as the main contributors of bribe payment should not be underestimated. Rules of corporate governance, such as accountability, transparency, and fairness, have profound

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