CORRUPTION, COMPETITIVENESS AND PUBLIC FINANCE IN EUROPEAN COUNTRIES

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Abstract

The paper discusses the relationship among corruption, competitiveness and public finance in the European countries. The influence of the corruption on the competitiveness and the economic performance is mentioned in the first part. Attention is given to the influence of the corruption on the economic environment and in particular possible impacts on public finance. The clean economic environment with low level of corruption is favourable for the economic performance and the public finance. The key hypothesis of the paper can be expressed this way: the competitiveness is high in countries with a clean economic environment even if there are high government expenditures and high taxes. Clean and transparent economic environment could be important as taxes and the volume of the government expenditures for public finance. The same argument applies to the competitiveness. The hypothesis is tested in the second part of the paper. The relationship between the level of the corruption and competitiveness as well as relationship between corruption and public finance is not possible unequivocally prove because CPI and CGI are based fully or partly on "soft" data. Nevertheless, the importance of clean economic environment is unchallengeable.

Key words: Corruption Perception Index, Global Competitiveness Index, Public finance

JEL Code: D29, E02, H70

Introduction

The public finance and budget deficit are discussed not only in the Czech Republic, but also in the other European countries. The budget deficit is of course caused by factors as economic growth, tax system, social policy and overall scope and system of government expenditures. The economic growth is influenced by the competitiveness, which is clear and commonly known fact. But the economic performance and competitiveness is influenced by institutional conditions. Corruption is one of circumstances affecting competitiveness and economic performance. The rate of corruption affects efficiency of public expenditures directly, but it has also an indirect impact.

"Corruption can be defined in different ways. However, the most common definition is that it is the abuse of public power to promote private benefits. Thus, a public employee who abuses his/her public position to derive benefits for oneself or friends, relatives or political associates is engaging in an act of corruption. Not all cases of corruption involve the payment of bribes" (Tanzi, 2003).

Because the corruption can be measured only with difficulties, there are data reflecting opinions of people and perception of the corruption used in the paper. The level of corruption is measured by the Corruption perception index (CPI) published by Transparency International.

Public finances are examined using data published by Eurostat.

1 Corruption and Public finance

As mentioned before, corruption affects public finance by direct and indirect way.
The direct influence of the corruption is clear: corruption affects effectiveness and also size of the public investment. Corruption can cause unnecessary public expenditures.

Corruption diverts public expenditures toward items on which is easier to levy bribes and maintain them secret (Mauro, 1998)

Corruption lowers growth through limiting development of small and medium sized enterprises, and has serious implications on public finances. Because entrepreneurs have to devote their scare time to bribing official, the growth promoting benefit o f small and medium sized enterprises is not fully realized. They estimate that due to this misuse of resources economic growth is lowered by 0,4 percentage points for a sample of countries (Tanzi, Davodi, 2000).

Studies IMF shows that both expenditure and revenue sides of budget are affected by corruption and rent seeking behaviour. Mauro shows that corruption is negatively associated with government expenditure on education: increase of corruption by one unit (on scale 1to 10) lowers the ratio of public spending on education by 0,2 percentage point of GDP. Corruption, therefore, could lead to suboptimal composition of government expenditure. Increase of corruption by one unit (on scale 1to 10), child mortality raises on average 1,1 to 2,7 deaths per 1000 live births (Marquette, 2003). It is reason why health and education outcome do not necessarily require higher public spending and taxes. These data reflect situation in less developed countries, but they show general fact: corruption decreases effectiveness of public spending and corruption reduces welfare in the final consequences.

Tanzi and Davodi argue that corruption distorts the composition of public expenditure. It leads to allocation in favour to less-productive investment project and against nonwage operations and maintenance expenditures , such as books and medicine., which reduce the quality and productivity of existing infrastructure. Corruption also reduces government revenue needed to finance productive spending (Tanzi, Davodi, 2000).

Gupta and Abed show that corruption is associated with higher military spending as share of both GDP and government spending. Military spending is a monopoly of the state, and contracts are often drawn in secrecy and under discretionary power of the authorities. Considerable amount of public spending takes place at subnational levels Gupta, M. S., & Abed, M. G. T. 2002). De Mello and Barenstein find that governance can be enhanced through the decentralization of expenditure functions to sub national government. The higher is the share of sub national spending in total government expenditures, the stronger positive association between decentralization and governance. The relationship between decentralization and poor governance also depends on how sub national expenditures are financed – the higher share of nontax revenues as well grants and transfers on higher levels of government in total expenditures, the stronger the association between decentralization and corruption (De Mello and Barenstein, 2001).

Hindrix, Keen and Muthoo find that the distributional implications of corruption are unambiguously regressive under most tax collection schemes, and that collecting progressive taxes without inducing evasion or corruption may require (Hindrix, Keen and Muthoo 1999).

IMF shows that both expenditure and revenue sides of budget are affected by corruption and rent seeking behaviour. Marquette contends that level of corruption influences the tax-revenue to GDP ratio. For a given tax regime and rate structure, measures taken curb corruption can be expected to raise tax revenues (Marquette, 2003). Corruption disrupts the structure of public expenditure. This causes concentration of public spending on less productive investments. That reduces the quality and productivity of the existing infrastructure. Corruption also lowers government revenues needed to finance productive spending.

2 Corruption and public finance (EU case)

Firstly we have to mention impact of corruption on economic performance. Some facts are commonly known about corruption in Europe. Corruption be love average in EU (average CPI in EU 67, world 43, source transparency international).

Corruption is usually lowest on the north and lower on west (Soukupová 2013). Higher corruption in post communist countries explains this phenomenon only partly. General statement that in "poorer" countries is usually higher level of corruption is observable also in Europe. Of course, it is possible find some exception, mainly if we focus

Tab. 1:Corruption perception index and Global competitiveness index

COUNTRY RANG 2015	COUNTRY RANG 2014	Country	CPI 2015 Score	CPI 2014 Score	GCI country	GCI rang 2015	GCI 2015 score
1	1	Denmark	91	92	Switzerland	1	5,76
2	2	Finland	90	89	Germany	2	5,53
3	3	Sweden	89	87	Netherlands	3	5,50
4	6	Netherlands	87	83	Finland	4	5,45
4	4	Norway	87	86	Sweden	5	5,43
6	4	Switzerland	86	86	United Kingdom	5	5,43
7	7	Luxembourg	81	82	Norway	7	5,41
7	8	Germany	81	79	Denmark	8	5,33
7	10	United Kingdom	81	78	Belgium	9	5,25
10	8	Iceland	79	79	Luxembourg	9	5,20
11	11	Belgium	77	76	France	11	5,13
12	13	Austria	76	72	Austria	12	5,12
13	12	Ireland	75	74	Ireland	13	5,11
14	14	Estonia	70	69	Iceland	14	4,83
14	14	France	70	69	Estonia	15	4,74
16	17	Portugal	63	63	Czech Republic	16	4,69
17	17	Poland	62	63	Spain	17	4,59
18	15	Cyprus	61	63	Lithuania	18	4,55
18	20	Lithuania	61	58	Portugal	19	4,52
20	20	Slovenia	60	58	Poland	20	4,49
21	19	Spain	58	60	Italy	21	4,46
22	25	Czech Republic	56	51	Latvia	22	4,45
22	22	Malta	56	55	Malta	23	4,39
24	22	Latvia	55	55	Romania	24	4,32
25	27	Croatia	51	48	Bulgaria	24	4,32
25	24	Hungary	51	54	Slovenia	25	4,28
25	26	Slovakia	51	50	Hungary	26	4,25
28	28	Greece	46	43	Cyprus	28	4,23
28	28	Romania	46	43	Slovak Republic	29	4,22
30	28	Italy	44	43	Croatia	30	4,07
31	28	Bulgaria	41	43	Greece	31	4,02

Source . CPI Transparency international http://www.transparency.org/cpi2015
GCI http://www3.weforum.org/docs/gcr/2015-2016/Global_Competitiveness_Report_2015-2016.

opposite side, there exists counties with high level of corruption between "richer" countries (Soukupová 2013).

If we look at public finance in EU, we can see examples of countries with

- low public debt and deficit and taxes[1] at average level or below average and lower share of government expenditure in GDP (example Estonia, Luxemburg but also Bulgaria and Romania)
- high public debt (above average) and average or low taxation example with higher share of government expenditure in GDP (example: Greece., Portugal,)
- low or average public debt and high taxation and high share of government expenditure in GDP (example: Denmark, Finland, Sweden, Germany)
- hight public debt and high taxation and high share of government expenditure in GDP Belgium, France, Italy,)

Czech republic and other Vishegrad four countries have not bad results in public debt and taxation is average or low in these countries, share of government expenditure in GDP is lover, exception is Hungary where share of government expenditure in GDP is above average.

Short look on public finance (tab 2) shows that there is no simple verifiable relationship between taxation and public debt and impact of corruption is not unequivocal. But one fact seems be clear. Countries with low level of corruption usually have no high public debt regardless taxation. One important phenomenon is considerable. Public expenditures and taxation are quite high without negative influence on public debt in countries with low level of corruption.

When we focused on competiveness, influence of corruption seems be more important. Countries with low level of corruption are successful in competiveness. It is not an unexpected fact; the level of corruption is one of the indicators influencing GCI. [2]Moreover, corruption is influenced by some factors important for competiveness, mainly by functioning institutions.

[1] Diferences in taxation are lovet than diferences in public debt

[2]

Tab.2:Government deficit, revenue

Country	General government gross debt % of GDP and million EUR		Total receipts from taxes and social contributions (percentage of gross domestic product)		Government deficit/surplus, debt (percentage of gross domestic product)		T Total general government expenditure (percentage of gross domestic product	
	2014	2015	2013	2014	2014	2015	2014	2015
EU (28 countries)	86,8	85,2	39,9	40,0	-3,0	-2,4	48,2	47,4
Euro area (19 countries)	92	90,7	41,2	41,5	-2,6	-2,1	49,3	48,6
Belgium	106,5	106	48,2	47,9	-3,1	-2,6	55,1	53,9
Bulgaria	27	26,7	27,9	27,8	-5,4	-2,1	42,1	40,2
Czech Republic	42,7	41,1	34,8	34,1	-1,9	-0,4	42,8	42,6
Denmark	44,8	40,2	48,1	50,8	1,5	-2,1	52,6	55,7
Germany	74,7	71,2	39,4	39,5	0,3	0,7	44,3	43,9
Estonia	10,4	9,7	31,7	32,5	0,8	0,4	38,0	39,5
Ireland	107,5	93,8	29,5	30,5	-3,8	-2,3	38,6	35,1
Greece	180,1	176,9	38,3	39,0	-3,6	-7,2	50,7	55,3
Spain	99,3	99,2	33,8	34,4	-5,9	-5,1	44,5	43,3
France	95,4	95,8	47,4	47,9	-4,0	-3,5	57,3	56,8
Croatia	86,5	86,7	36,6	36,7	-5,5	-3,2	48,1	46,9
Italy	132,5	132,7	43,6	43,7	-3,0	-2,6	51,2	50,5
Cyprus	108,2	108,9	31,6	34,2	-8,9	-1,0	48,7	40,1
Latvia	40,8	36,4	28,7	29,2	-1,6	-1,3	37.5	37,2
Lithuania	40,7	42,7	27,4	28,0	-0,7	-0,2	34,8	35,5
Luxembourg	22,9	21,4	39,5	39,4	1,7	1,2	42,4	41,5
Hungary	76,2	75,3	38,2	38,4	-2,3	-2,0	49,8	50,7
Malta	67,1	63,9	33,6	35,0	-2,0	-1,5	43,2	43,3
Netherlands	68,2	65,1	37,2	38,0	-2,4	-1,8	46,2	44,9
Austria	84,3	86,2	43,3	43,8	-2,7	-1,2	52,5	51,7
Poland	50,5	51,3	32,8	33,0	-3,3	-2,6	42,2	41,5
Portugal	130,2	129	37,2	36,9	-7,2	-4,4	51,7	48,3
Romania	39,8	38,4	27,4	27,7	-0,9	-0,7	34,3	35,5
Slovenia	81	83,2	37,3	37,0	-5,0	-2,9	49,9	48,0
Slovakia	53,9	52,9	30,3	31,2	-2,7	-3,0	41,9	45,6
Finland	59,3	63,1	43,9	44,0	-3,2	-2,7	58,1	58,3
Sweden	44,8	43,4	43,8	43,7	-1,6	0,0	51,7	50,4
United Kingdom	88,2	89,2	34,9	34,4	-5,6	-4,4	43,9	43,2
Iceland	:	:	36,0	38,9				42,7
Norway	27,3	31,6	39,9	38,9	8,7	5,7	45,6	48,5
Switzerland	:	:	27,1	27,1			33,7	

Source: Eurostat

Conclusion

Corruption affects economic and social environment and also public finance. Impact of corruption could be direct through public spending and indirect through economic performance.

Reducing government spending is often recommended as way to reduce corruption and improve public finance. Of course, that recommendation is completely right. But example of north Europe shows that institutional factors reducing corruption may be also important. Although these factors is not possible easily and quickly be changed, focus on them is one of opportunities to improve public finances and economic performance in many countries.

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