

Does Economic Freedom Influence Governmental Corruption? An Empirical Analysis

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In this study, I ask the question: does economic freedom influence governmental corruption around the world? In response to this question, I hypothesize that economic freedom does influence the rates of governmental corruption in countries around the world. Upon conducting research, I found a strong correlation and a statistically significant relationship between economic freedom and governmental corruption. Other factors not accounted for in this study (e.g.: education, economic development, and regime type) tend also to play a moderate role in the levels of governmental corruption in countries around the world.

Literature Review

Some may question why determining the factors that contribute to governmental corruption is a necessary task. Corruption in government can contribute to a multitude of secondary issues within a country, including poverty rates, death rates, hostility with other

countries, civil war, and national debt (see Kumar for instance). One article, by the Institute for Research in Economic and Fiscal Issues (IREF), states that “corruption has a negative impact not only on GDP and economic growth, but also on the volume of investments as well as life expectancy in a country” (Fink, 2016). Another report on corruption found that “country level data [shows] high levels of corruption are strongly correlated with low GDP and GNP per capita, low average education attainment, and low achievement on most other development indicators” (Kaffenberger, 2011: 1). Other research reports that “governments, the international community, and NGOs have devoted millions of dollars to anti-corruption programs and policies in order to fight corruption and curb its negative effect” (Zakaria, 2018). Understanding the factors that contribute to governmental corruption may lead to the implementation of preventative measures or policies.

Researchers with the IREF, likewise, assert that “corruption tends to be less common in countries with higher levels of economic freedom” (Fink, 2016). According to Richard M. Ebeling (2017), a professor of Ethics and Free Enterprise Leadership and former president of the Foundation for Economic Education (FEE), “in a generally free market society, government is limited to the protection of the citizenry’s life, liberty, and honestly acquired property,” leaving little opportunity or incentive for bribery and other forms of corruption. An article from the Heritage Foundation echoes the same sentiment, stating that “some government action is necessary for the citizens of a nation to defend themselves and to promote the peaceful evolution of civil society, but when government action rises beyond the minimal necessary level, it is likely infringing on someone’s economic or personal freedom,” and therefore contributes to governmental corruption (“Economic Freedom: Policies”). The definitions of corruption put forth by Ebeling and the Heritage Foundation contrast it with the traditional features and values of democracy, including transparency, fidelity, and equality, which are consistent with an uncorrupt form of government.

Many other scholars have reached the same conclusion, that an increase in economic freedom directly contributes to a decrease in governmental corruption. Information provided by the Heritage Foundation describes the consequential relationship between highly regulated economies and a government's propensity to act corruptly. An analysis from this think tank explains that "by imposing numerous burdensome barriers to conducting business, including regulatory red tape and high transaction costs, [a] government can incentivize bribery and encourage illegitimate and secret interactions that compromise the transparency" of the nation and its government, undertaking a contributory role in the rampant corruption of government ("Economic Freedom: Policies"). A study from the Center for Civil Society took an empirical approach in demonstrating the relationship between economic freedom and governmental corruption. It found a negative correlation between the two variables, such that "a unit increase in economic freedom led to a decrease by 3.73 standard deviation, in corruption" (Kumar, 2011: 11). In sum, the foregoing studies seem to suggest that the relationship between high economic freedom and low governmental corruption is not just a theoretical conjecture but also one that can be demonstrated empirically.

Model Specification

For the purpose of this study, the level of economic freedom, the independent variable, is defined as the degree to which "governments allow labor, capital, and goods to move freely, and refrain from coercion or constraint of liberty beyond the extent necessary to protect and maintain liberty itself" ("2020 Index of Economic Freedom"). Governmental corruption, the dependent variable, is understood as any illegal and/or unethical act committed by a member[s] of a government in regards to their professional duties. These acts include bribery, the diversion of public funds, using public office for private gain, creating red tape and excessive

bureaucratic burden to hide corruption, nepotistic appointments rather than meritoric appointments, and similar offenses (“Corruption Perception Index 2019”).

The economic freedom of each country within the sample group is ranked on a scale of 0.0-100.0, where 100.0 represents the highest level of economic freedom possible and 0.0 represents the lowest level of economic freedom possible. The level of governmental corruption is measured in a similar manner, on a scale of 0.0 to 100.0. For the index of governmental corruption, a score of 0.0 indicates a highly corrupt government, and a score of 100.0 indicates a country completely free of governmental corruption.

Despite the general consensus that economic freedom contributes to a decrease in governmental corruption, there are additional variables that a study like this should control for. For instance, Ebeling asserts that although economically free systems of government leave little room for governmental corruption, he also states that the relationship between the two variables is “not one-to-one.” Rather, he cautions that “there are many variables at work” that can influence corruption in governments around the world. Ebeling is not alone in his concern. The Center for Civil Society provides a similar caveat, stating that the relationship between the two variables “needs to be studied with several other factors that are found in real life and affect this relation” (Kumar, 2011: 15).

The guidance of the foregoing researchers suggests that it would be worthwhile to take additional variables into consideration when examining governmental corruption. Such control variables include education level, economic development, and regime type of countries. For instance, “education has been shown to reduce illegal behavior, decrease arrest rates, improve social cohesion, and increase civic responsibility,” contributing to a decrease in both personal and governmental corruption (Kaffenberger, 2012: 3). More generally,

“higher education rates are associated with lower levels of corruption for a range of...indicators” (Kaffenberger, 2012: 15).¹

In regards to economic development, a report from the National Bureau of Economic Research found that “economic growth...reduces the proportion of firm revenues extracted by government officials as bribes” and can, therefore, contribute to a decrease in certain forms of governmental corruption (Bai, Jie et al., 2013).

Finally, the regime type of a country may also affect its level of governmental corruption. According to research conducted by Dr. Patty Zakaria (2018), a research manager and faculty member for the University of Canada who specializes in the effects of socialization on corruption toleration, “several studies [confirm] that regime type has a significant influence on corruption levels in [countries]” around the world. For instance, democracies tend to foster a culture of transparency and fidelity (Ebeling, 2017).

For this study, the sample size is 50 countries, selected randomly from around the world. The data for economic freedom were collected from the “Index of Economic Freedom” provided by the Heritage Foundation, a recognized think tank that specializes in public policy issues. The Heritage Foundation’s Index is “based on 12 quantitative and qualitative factors, grouped into four broad categories, or pillars, of economic freedom.” These categories are:

- Rule of Law (property rights, government integrity, judicial effectiveness),

¹ The relationship between educational attainment and corruption is also revealed to have a reciprocal effect, as high levels of governmental corruption are shown to infiltrate and trickle over into systems of higher education, injuring the capability for high educational attainment in certain cases (Orkodashvili, 2009). In addition, another research has found that higher levels of education strongly correlated with high levels of corruption, perhaps due to “corrupt education systems and the higher returns to bribery that education brings,” which is largely due to a “higher value of time” and increased “interaction with officials” among those with more education (Kaffenberger, 2012: 44-45).

- Government Size (government spending, tax burden, fiscal health),
- Regulatory Efficiency (business freedom, labor freedom, monetary freedom),
- Open Markets (trade freedom, investment freedom, financial freedom).

The data for governmental corruption were collected using the “Corruptions Perception Index” created by the Transparency International Organization. Their measurements were developed through “13 data sources from 12 independent institutions specialising in governance and business climate analysis.”

Between the two sources, the years of analysis lie between 2017 and 2019, with 2019 being the primary year of study. For the “Corruptions Perception Index,” the data were for a two year period, 2017 through 2019. The data for the “2020 Index of Economic Freedom” cover information that was current between the second half of 2018 and the first half of 2019.

Research Design

The procedure I used to test the relationship between economic freedom and governmental corruption in countries around the world is a regression analysis (ordinary least squares, OLS, regression estimators). This method was chosen because variables measured with interval level data, such as the data used for economic freedom and governmental corruption levels, are best estimated by using the OLS estimators. The results of the data and all relevant conclusions are described below.

Model Estimation and Analysis

The OLS model used in this research study is given by the following equation:

$$Y = a + bX + e; \quad \text{where}$$

Y = the dependent variable
 a = the Y-intercept
 b = the slope
 X = the independent variable
 e = the error term

My data analysis of economic freedom and governmental corruption in countries around the world provided the following equation of the regression line and additional data using the SPSS module:

$$Y = (-13.300) + 0.975X$$

$$t = 7.534; p = 0.000; R^2 = 0.542$$

Because the t value, 7.534, is greater than 2.0 and the p value, 0.000 (less than 0.001), is less than 0.05, we can say that there is a statistically significant causal relationship between economic freedom and governmental corruption for countries around the world. In other words, the data seem to suggest that one can be 95% confident in rejecting the null hypothesis. That is, we can safely assume that there is relationship between economic freedom and governmental corruption.

In addition, the Y-intercept, (-13.300), suggests that when a country has no economic freedom, the index of governmental corruption is -13.300. In this case, because an index of 0 indicates a highly corrupt government, the Y-intercept suggests that a country with no economic freedom is extremely corrupt. The slope, 0.975, suggests that for every one unit increase in economic freedom, a country's index of governmental corruption decreases by 0.975 points.

A further examination of the data, including the scatterplot, suggests that there is a healthy correlation between economic freedom and governmental corruption--in which an increase of economic freedom correlates with a decrease in governmental corruption. More specifically, the Pearson's coefficient, R , is 0.74. Because this value is

grater than 0.60, the correlation between the index of economic freedom and index of governmental corruption in countries around the world is said to be relatively strong.

The R-squared value, 0.542, suggests that about 54% of the variance or difference in the governmental corruption of countries around the world is explained by the variance or difference in the level of their economic freedom. Approximately 46% of the index of governmental corruption is explained by other variables, variables that were not included or controlled for in this study.

Conclusions

This paper sought to answer the following question: Does economic freedom influence the levels of governmental corruption in countries around the world? To address this question, I hypothesized that economic freedom does, in fact, influence corruption in governments of countries around the world. My study found that the relationship between economic freedom and governmental corruption are highly correlated and statistically (or causally) significant. Generally, an increase in economic freedom and a decrease in governmental corruption go hand in hand; however, the assertion that increased economic freedom *causes* a decrease in governmental corruption can only be stated with a confidence so long as we acknowledge that other factors have additional influence on this dependent variable.

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Country	Econ.Freedom	Gov.Corruption
Mexico	66.0	29.0
Suriname	49.5	44.0
United States	76.6	69.0
Sri Lanka	57.4	38.0
Bosnia & Herzegovina	62.6	36.0
Cuba	26.9	48.0

Burkina Faso	56.7	40.0
India	56.5	41.0
Brazil	53.7	35.0
Spain	66.9	62.0
Romania	69.7	44.0
Denmark	78.3	87.0
Qatar	72.3	62.0
Kazakhstan	69.6	34.0
Morocco	63.3	41.0
Vanuatu	60.7	46.0
Ghana	59.4	41.0
Nepal	54.2	34.0
Chad	50.2	20.0
Sierra Leone	48.0	33.0
Venezuela	25.2	16.0

Moldova	62.0	32.0
Luxembourg	75.8	80.0
South Africa	58.8	44.0
Egypt	54.0	35.0
Ireland	80.9	74.0
Guatemala	64.0	26.0
New Zealand	84.1	87.0
Latvia	71.9	56.0
Kenya	55.3	28.0
Turkmenistan	46.5	19.0
China	59.5	41.0
Georgia	77.1	56.0
North Korea	4.2	17.0
Hong Kong	73.3	76.0
Estonia	77.7	74.0

Netherlands	77.0	82.0
Australia	82.6	77.0
Poland	69.1	58.0
Afghanistan	54.7	16.0
Hungary	66.4	44.0
Mongolia	55.9	35.0
Cyprus	70.1	58.0
Bolivia	42.8	31.0
Tunisia	55.8	43.0
Cameroon	53.6	25.0
Rwanda	70.9	53.0
Cabo Verde	63.6	58.0
Iceland	77.1	78.0
Madagascar	60.5	24.0

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.736 ^a	.542	.532	13.65300

a. Predictors: (Constant), Econ.Freedom

Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-13.300	8.174		-1.627	.110
	Econ.Freedom	.975	.129	.736	7.534	.000

a. Dependent Variable: Gov.Corruption

