

# **Does privatization influence corruption perceptions?**

## **Evidence from Latin America**

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### **Extended Abstract**

This paper analyses the effects of privatization satisfaction on corruption perceptions. In Latin America there is a paradoxical situation, where welfare gains of pro-market reforms have not been translated into individuals' levels of privatizations satisfaction. Corruption could be explaining this gap.

It is naïve to expect that actual corruption measures can be easily determined. Therefore, real observations of corruption are almost impossible to obtain. For that reason, most current empirical studies on corruption base their analysis on subjective measures, such as surveys on perceived levels. Data is normally obtained through mass media and organizations such as the World Bank (WB) or Transparency International (TI). Since the main conclusions of corruption's causes and consequences are founded on perceptions, it is important to establish what these are. If their determinants are known, it will allow a more precise analysis of which individuals are more affected by corruption and why.

There are some factors which may have an important impact on the perceptions of corruption but which have not been previously considered. An interesting example to

consider here is the wave of privatizations that took place in Latin America over the past two decades. Despite the fact that pro-market policies have proved to be an important success in terms of efficiency or welfare, there has been an increasing rejection of privatization processes from public opinion. Several studies have tried to explain this paradox and some researchers argue that the lack of transparency in the application of privatization programs implies the fact that citizens tend to distrust the outcomes.

During the same period, an analysis of Latin Americans perceptions indicates that they believed there was an increased corruption, and this suggests that there may be a link between the two levels of reported perceptions. As far as we are aware, there are no existing empirical studies to explain corruption reported levels as a function of satisfaction with privatization reforms. Accordingly, this is precisely the question this paper proposes to pursue: have pro-market reforms influenced Latin Americans' perceptions of corruption?

In order to perform our analysis we use *Latinobarómetro* surveys for the years 1998-2005. We complement this data with macro level variables, in order to account for the different economic, political and institutional country traits that can affect corruption perceptions. Finally, we end up with more than 120,000 individual observations, for 17 Latin American countries.

With this database, we are able to estimate the effects of privatization opinions on corruption perceptions. The fact of considering corruption the main important problem is the principle dependent variable that we take into account. However, other corruption perceptions measures are also used, such as the degree of seriousness perceived by the respondent or the opinion on the evolution of corruption.

We use two different methodologies to carry out our analysis. Firstly, we estimate a probit model which accounts for the non linear behaviour of corruption perceptions. Secondly, we also estimate a Linear Probability Model (LPM), where we can control for country and year fixed effects.

Both methods confirm our hypothesis: opinions about corruption have an impact on corruption perceptions. More precisely, dissatisfaction with privatizations can imply an increase of 0.5 to 0.8 per cent on the average probability of considering corruption

the main problem, keeping all other regressors constant. For the probit model, the value of the marginal effect is almost the same, 0.8 to 0.9.

Nonetheless, we should bear in mind that these models can suffer from an omitted variables bias as well as an endogeneity problem in the measure of privatization opinions. In order to account for the unobserved heterogeneity of the respondents we include in the analysis beliefs regarding the state of the economy and its evolution. Also, we instrument privatization opinions using as a set of exogenous variables the respondent's political orientation and their opinion about the determinants for life success. Literature on privatization satisfaction supports the validity of these variables, and it is assessed by formal tests.

The bivariate probit estimation and the instrumental variables linear regression confirm the suspicion that privatization opinions are endogenous in our estimating equations and, therefore, they considerably raise our previous results. With the use of adequate techniques and instruments, privatization satisfaction increases up to 30% the probability of considering corruption the most important problem of the country.

We also perform the analysis using different dependent variables as a check for robustness in order to confirm previous results. Several tests are implemented to verify the validity of the instruments utilised, as well as the suitability of the different estimations.

Our results contribute to existing economic and political science literature that explains the gap between privatization outcomes in Latin America and satisfaction levels perceived by citizens. As previously demonstrated, Latin American's reported levels of corruption are highly influenced by their opinions on pro-market reforms, which could be the result of those irregularities perceived in the implementation of these processes.