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The end of a beauty pageant for investors

The World Bank's Doing Business Index was manipulated to push neoliberal policies. Now it will finally be discontinued

Read this article in German.

It was about time. The World Bank has finally discontinued publishing its 'Doing Business' index (DB). The index assessed the business environment in individual countries and rated their attractiveness for foreign investment. Now the World Bank has conceded 'irregularities' in its data, which could have influenced the rankings of emerging markets. With governance indicators long criticised, it was past time to discontinue the index.

Since 2003, DB indices had been published annually by the International Finance Corporation (IFC), an international development bank within the World Bank Group focused on the private sector in developing countries. Like the Index of Economic Freedom compiled by the conservative Heritage Foundation, DB was designed to promote deregulation, with its ideology based on 1970s and 1980s tenets.

Back then, legal institutions were seen as influencing economic growth and countries that following English common law were expected to fare better than countries with civil laws. In the heyday of Thatcher and Reagan, economists used it as a benchmark.

Deregulate everything

The DB index was like a global beauty pageant for investors. Its Ease of Doing Business ranking calculates the gap between a particular economy's performance and 'world best practice' – as defined by the IFC. That calculation was then used to determine an international DB ranking: It assessed the difficulty in 'starting a business, dealing with construction permits, getting electricity and credit, enforcing contracts

and resolving insolvency.' Registering property, paying taxes and trading across borders were also assessed.

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According to the IFC, in recent years the DB index had driven many emerging and developing countries to improve their business environments and dispose of 'regulatory ballast'. In fact, the governments of some emerging markets even calibrated the index on their websites to attract investors.

Deregulating labour markets – in other words, making it easier to sack employees – was always appreciated. However, after the International Confederation of Free Trade Unions (ICFTU) protested, it was removed from the DB ranking. The ICFTU and numerous unions accused the bank of misusing the DB to persuade governments to implement lower minimum wages and ditch their duty to give advance notice of mass layoffs. During the great recession of 2009, the World Bank finally agreed to exclude the labour market flexibility indicator.

A corrupted indicator

According to the IFC website, the last DB report included India, Nigeria and Saudi Arabia among the major economies to have most markedly improved their business environments; New Zealand, Singapore and Hong Kong top the 2020 rankings. Germany (22), Switzerland (36) and the Netherlands (42) lag quite far behind European countries like Georgia (7), North Macedonia (17) and Latvia (19). What accounts for these astonishing results?

For one thing, a narrow focus on regulatory practice ignores macroeconomic stability, sustainable competitiveness, respect for the rule of law and the employees' educational level. Moreover, DB reports rely on surveys conducted by management consultants and law firms rather than by companies engaged in productive activities, whose needs are generally different from the report's ideological prerogatives. Lastly, the DB rating has become increasingly corrupted politically.

Once again Campbell's Law applies: 'The more any quantitative social indicator is used for social decision-making, the more subject it will be to corruption pressures and the apt it will be to distort and corrupt the social processes it is supposed to monitor.' Performance indicators and rankings are 'political figures' that ostensibly stand for rational decision-making. Preliminary political decisions and dubious assertions determine how a society that trusts in numbers can maintain the illusion that

politics are superfluous, since 'facts' lead to the right decisions and the market decides the direction.

An opportunist methodology

In early 2018, World Bank Chief Economist Paul Romer told *The Wall Street Journal* that he had lost faith in the integrity of the Doing Business index. The DB had been politically manipulated to embarrass Chile's socialist president, Michelle Bachelet. As a report of the Center for Global Development put it: 'Questionable methodological changes had made Chile's ranking plummet after Bachelet took office, then rise again under her conservative successor Sebastián Piñera, only to crash a second time when Bachelet returned to power in 2010 – through manipulating the methodology and absent any fundamental changes to Chile's laws or policies.'

Chile was no fluke. India's rise in the DB rankings, which were celebrated by Prime Minister Narendra Modi ('The biggest democracy in the world is also the fastest growing economy!'), proved to be largely due to methodological changes (to get India's fantastic growth figures). India's rank only rose because of new indicators, while Saudi Arabia shot up in the rankings of the 2019 Doing Business report after buying lots of weapons from the US.

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Not only are governance indicators susceptible to abuse but they also fail – for a variety of reasons. In international comparisons, a correlation can be found between 'good governance' and the level of GDP per capital. But there is *no correlation with the speed of development*, of medium to long-term growth. Why not? Popular governance indicators, including those used by the 'G20 Compact with Africa', such as the Bertelsmann Transformation Index, largely reflect the level of development of wealthy Western economies.

However, they shed little light on the driving forces behind institutional, economic, political and social changes. Politicians are not interested in nuance: They just use international rankings to back up their arguments. But any ranking can be cited to substantiate any claim – and none of them are scientific.

Time to try something different

An especially harmful DB indicator aimed at global investors encouraged poor countries to keep their taxes low and to only marginally regulate them. The DB instigated a kind of race to the bottom for poor countries – signaling that the winners would be rewarded with foreign direct investment. For investors, however, stability, reliability and regulatory clarity are more important than tax rates.

'Doing Business' often creates the wrong incentives, such as by rewarding the countries that have low taxes. At the same time, the World Bank calls on developing countries to better mobilise their domestic resources to finance their expenditures and not depend on foreign aid. Nonsense! A country like Nigeria, whose taxes amount to almost six per cent of gross domestic product, needs *more* tax income – not less – to develop.

In 2013, an independent review panel set up by the World Bank under South Africa's Planning Minister Trevor Manuel recommended discontinuing the DB aggregate index. It also recommended no longer publishing indicators of labour market flexibility and tax rates.

The latest scandal should serve to reorient future DB reports to take into account the development perspective – especially for poor countries. Macroeconomic stability, legal certainty, the quality of the infrastructure, the level of educational, corruption… – all *these* have been missing. The UN Human Development Index and the OECD's Better Life Index, used to present quantitative overall impressions, are good models.



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