

# Celebrating reform

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Name your favorite dentist. Don't have one? That's because no one likes going to the dentist. Sometimes he gives you unpleasant news. Sometimes it hurts. Once you are healthy you stay as far away for as long as possible.

Reformers are like dentists. Necessary, but generally disliked. Their job is to cure the economy and create jobs. Very often this involves unpleasant news and it hurts, initially. In fact, reformers are even worse off than dentists: they are disliked even by their own kind. When a reformist minister says commercial disputes need to be resolved faster in the courts, the justice minister accuses him of ignorance. Or arrogance. Or both. When a reformist minister says labor regulations are too rigid and leave many people stranded in the informal economy, the labor minister accuses him of ignorance. Or arrogance. Or both.

In prosperous times, reformers are told not to rock the boat. In crisis times, they get the blame for not reforming sooner and averting the crisis. Some pursue reforms while receiving personal threats and threats to their families. It is hard to be a reformer.

Here are 3 ways to change that. First, document successful reforms and the challenges that had to be overcome along the way. This helps future reformers and highlights the contributions of past ones. Second, create a prize to recognize reformers. Movies have the Oscars, science has the Nobels, and sports have the Olympics. Reformers can have awards too. Finally, encourage reformers to write up their often dramatic stories. Imagine if these were turned into movies. It would only take a few films starring Jude Law, Angelina Jolie and George Clooney to make reformers more popular.

*Doing Business* develops the first idea, by presenting 8 case studies of recent reforms. These span the globe—from Serbia to El Salvador, from Egypt to Nigeria—and show what it takes to succeed. The case studies show several patterns: Reforms usually happen when new governments take office. They often follow crises. Reformers don't have time for concepts like "getting the right sequencing" and "finding the binding constraint." Reformers are helped by active media and information campaigns. And reforms may benefit from tapping development experts, outside expertise (be it from ISO9000 inspectors or Microsoft's software engineers), and lessons from other countries.

We also take on the second idea, by organizing the first annual awards for outstanding reformers (details available at [www.reformersclub.org](http://www.reformersclub.org)). The third idea is waiting for its champion.

## Reforms are on the rise

Reforms to make it easier for businesses to operate are on the rise. In 2005-06, 213 reforms took place in 112 countries. This compares to 185 reforms in 99 countries in 2004-05. And 89 reforms in 58 countries in 2003-04.

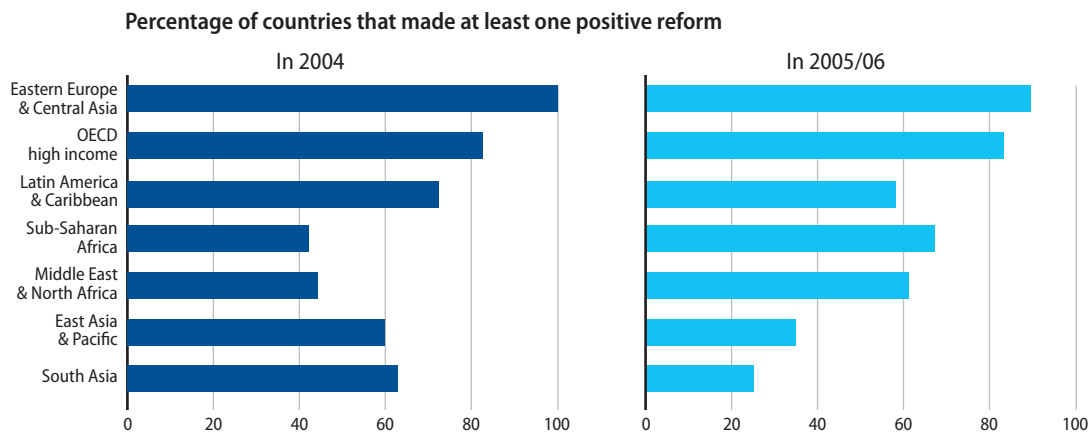
Four reasons explain the upswing. First, the collapse of socialism and the entry of Eastern Europe and the former Soviet Union in the world economy. Over the last decade, this region has led in reforms (figure 1). This is not surprising: the environment for doing business in the private sector was difficult so a lot had to be changed.

Second, the increase in global and regional competition. Regional agreements such as the US free trade agreements with Central American countries and accession of Eastern European countries into the European Union (EU) have generated huge reform momentum. Also, China has become everyone's competitor. In 2005-2006, 4 of the top-10 reformers have reformed to enter regional agreements: Croatia, Guatemala, Peru and Romania. China was a top reformer too (table 1). Countries are competing for investment, enterprises, and the jobs that come with them—and as a result it is getting easier to do business around the world.

Third, a new focus on reducing corruption. Many reforms to business regulation are made not to increase efficiency but to cut the corrupt practices of government officials. This is illustrated most vividly by Georgia, the top reformer in *Doing Business 2007* and also the country achieving the biggest drop in corruption in all of Europe—in 2002 37% of businesses said that they frequently paid bribes compared with only 8% in 2005.

FIGURE 1

### The pace of reform is strong in most regions outside of Asia



Source: *Doing Business* database.

TABLE 1

**The top 10 reformers in 2005/06**

Economy	Starting a business	Dealing with licenses	Employing workers	Registering property	Getting credit	Protecting investors	Paying taxes	Trading across borders	Enforcing contracts	Closing a business
Georgia	✓	✓	✓		✓			✓	✓	
Romania		✓	✓		✓	✓		✓		✓
Mexico	✓					✓	✓			
China	✓				✓	✓		✓		
Peru	✓				✓	✓			✓	X
France		✓			✓			✓	✓	✓
Croatia	✓			✓					✓	
Guatemala	✓	✓		✓						
Ghana				✓			✓	✓		
Tanzania	✓			✓		✓		✓		

Note: Economies are ranked on the number and impact of reforms. First, *Doing Business* selects the economies that reformed in 3 or more of the *Doing Business* topics. Second, it ranks these economies on the increase in rank in the ease of doing business from the previous year. The larger the improvement, the higher the ranking as a reformer. "X" indicates a negative reform.

Source: *Doing Business* database.

Finally, what gets measured gets done. New indicators on business regulations in *Doing Business*—and from other sources—allow countries to identify bottlenecks and compare their performance with competitors. This inspires competition—no one likes looking worse than their neighbors. In 2000, EU countries agreed to track the time and cost to start a business. Since then, every EU country has made startup easier. The effect is even stronger when measurement is linked to financial incentives. When the United States' Millennium Challenge Account (MCA) made eligibility for funding dependent on the ease of business startup, countries from Burkina Faso to El Salvador to Georgia to Malawi started reforms. Indonesian Finance Minister Sri Mulyani Indrawati argues that the real impact of the MCA is its "good housekeeping seal of approval," which sends a powerful signal to investors. "It's not about the money. It's about the recognition that we're doing the right thing."

## How reforms are done

The existing manuals on reforms offer a simple recipe: take a strong reform champion, mix in highly-qualified technical staff, throw in valuable advice from development experts, stir it just the right amount of time, and serve while still hot. The problem is that reformers often miss some ingredients and the results can be a bit lumpy. Here are some ideas on substitutes.

A lot of reforms are sparked by crisis. But there's no need to wait for one to get change—crises always make things more painful. Reformers can create a sense of urgency to motivate change—in Nigeria, people were shocked when reformers publicized findings that 99% of lawyers agreed the judiciary was corrupt. In Mexico, reformers used the Enron and WorldCom scandals in United States to push through higher Mexican corporate governance standards. In 2004, at the start of tax reforms, Egyptian Finance Minister Youssef Boutros-Ghali pointed to weakening government finances and said, "Doing nothing is definitely not the solution. The greatest enemy to reforms is inertia."

We know nearly 85% of reforms in top reforming economies took place in the first 15 months of a new government. But even without a new political mandate, reformers can achieve a lot by simplifying administrative procedures. When the government succeeds in early reforms, citizens start seeing benefits—more jobs, more resources for health and education. The appetite for further reforms grows. Unable to make legislative changes easily, El Salvador cut the time to start a business from 155 days to 26 within 2 years—all through administrative reforms at the company registry. Now they are working on the law. Reformers in Pakistan implemented administrative reforms immediately while preparing the ground for the more difficult and costly longer term reforms. One of Kenya's reformers notes, "If we had waited for laws to do a number of things we're doing, we would not be doing them."

Ask development agencies about reform strategies and they'll likely talk about addressing the binding constraint to growth or sequencing the reforms efforts. Ask a successful reformer and they'll talk about seizing the opportunity, any opportunity. "Reform is like repairing a car with the engine running," says Mahmoud Mohieldin, the Egyptian minister of investment. In Nigeria it did not take years of strategizing before reforming the courts. Ten months after a new attorney-general of Lagos State took office, 26 new judges were appointed, specialized commercial divisions set up, and judges' salaries increased. In another example, property registration was reformed in Georgia in 4 months following the Rose Revolution. The previous government had spent 6 years going through the motions of commissioning studies, consulting with experts, and sponsoring seminars.

The strongest opposition usually comes from within. In Pakistan, customs workers were unhappy with the introduction of more efficient procedures and tried to subvert reform. In Mexico, a prominent media tycoon lobbied for weakened disclosure laws. In Serbia and Bulgaria, the ministers of justice did not want to yield power to more efficient company registries. In Peru, a modernized collateral registry promised to help borrowers but threatened the business of notaries, who protested loudly and managed to derail the reforms. In several European Union countries, notary associations lobby against the adoption of electronic signatures—which has vast potential to simplify bureaucracy. (This may change: recently the European Commission filed anti-competitiveness charges against 9 notary associations.)

Once you design the reforms well, the next way to overcome opposition is with a smart outreach campaign: telling people these are the reforms we are doing and this is how they are going to help you. But most reformers don't spend enough time on outreach. Opposition builds and few entrepreneurs grasp how much easier life can be after the reforms. El Salvadorian reformers worked with the media to explain and build support for the changes. Other reformers bargained directly with stakeholders. In Macedonia, labor unions were at first deeply opposed to the reform. But once they were brought into the reform process, they worked with the government and employers to improve regulation. Key to making the reform work was including the unions in the drafting of the new law.

Sometimes, a reformer even manages to convince the opposition. In Serbia, study tours for bankruptcy judges benefited the reform effort as much as they benefited the judges: “For every dime we spent on the tours, we saved tenfold from not having to spend money on overcoming resistance from the judges. They were welcoming the new law instead of fighting it.” One USAID expert said that the study tours bolstered the credibility of reformers in the Ministry of Economy, as judges could “feel and taste and smell” for themselves and were more convinced that what they were being told could be put into practice.

Reformers can also blame changes on outsiders. It is no accident that Eastern Europe is the fastest reforming region. Reformers there could push through controversial changes by saying that the EU requires them. And El Salvador used access to the MCA as a reform rationale.

Sometimes a reformer needs luck. A fluke of timing helped Mexico overhaul its securities laws, a reform that *Doing Business 2007* named “Reform of the Year.” “We finished drafting the bill in March 2004, too late to submit to Congress that term. But instead of waiting until October, we decided to show it to people in the private sector,” relates José Antonio Gonzalez, director general for Securities and Insurance in the Ministry of Finance and a key drafter of the new law. “Their input made all the difference.”

All reformers gain from using indicators that allow them to monitor progress and change course when needed. In Nigeria, the National Judicial Council announced ratings of judicial performance in May 2006. Judges now know they are being monitored by an institution with disciplinary power. The poorest performers have already left the bench. In El Salvador constant customer feedback on ideas about improved efficiency was crucial in measuring success of the reforms and identifying what was still missing. With clients as the evaluators of performance, reforms quickly became more appreciated—and customer-orientation became more than a buzzword.

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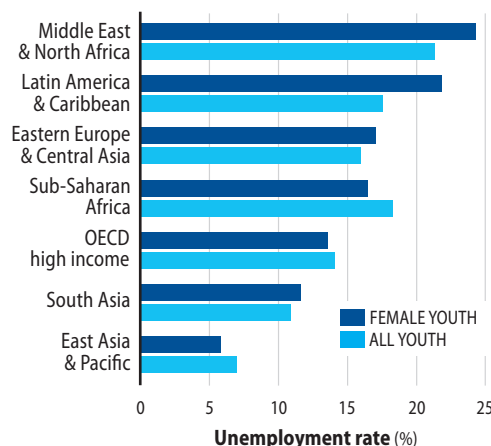
### **Who benefits from reform**

In Bolivia 400,000 workers have formal jobs in the private sector—out of a population of 8.8 million. In India 8 million workers have such jobs—in a country of 1.1 billion people. In Malawi, 50,000 out of a population of 12 million. In Mozambique, 350,000 in a country of 20 million.

Reform can change this, by making it easier for formal businesses to create more jobs. Women and young workers benefit the most. Both groups account for a large share of the unemployed (figure 2). Reform also expands the reach of regulation by bringing businesses and workers into the formal sector. There, workers can have health insurance and pension benefits. Businesses pay some taxes. Products are subject to quality standards. And businesses can more easily obtain bank credit or use courts to resolve disputes.

Between 2002 and 2006 Slovakia's reforms have helped cut the number of unemployed people by 67,000. In Colombia reforms of employment and business startup regulations have created 300,000 jobs in the formal economy. Another success story comes from Peru, where in the past decade the government has issued property titles to 1.3 million urban households. Secure property rights have enabled parents to find jobs rather than staying home to protect their property. Similarly, children can now attend school. As a result, the incidence of child labor has fallen by nearly 30%.

FIGURE 2  
**High unemployment among youth, especially females**

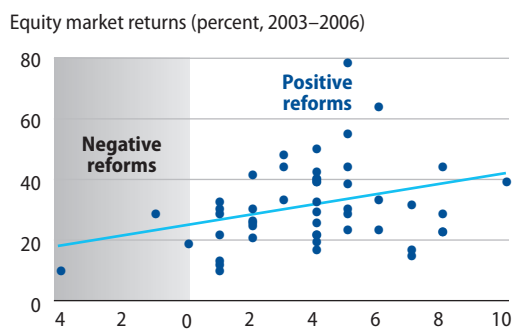


Source: ILO (2005).

A hypothetical improvement on all aspects of the *Doing Business* indicators to reach the level of the top quartile of countries is associated with an estimated 1.4 to 2.2 percentage points in annual economic growth. This is after controlling for other factors, such as income, government expenditure, investment, education, inflation, conflict, and geographic regions. In contrast, improving to the level of the top quartile of countries on macroeconomic and education indicators is associated with 0.4 to 1.0 additional percentage points in growth.

The gains come from 2 sources. First, businesses spend less time and money on dealing with regulations and chasing after scarce sources of finance. Instead, they spend their energies on producing and marketing their goods. The association between reforms and more profitable businesses is best seen in the increase in equity market returns (figure 3). Second, the government spends fewer resources regulating and more providing basic social services.

FIGURE 3  
**More reforms, higher equity returns**



Source: MSCI, available at [www.msccibarra.com](http://www.msccibarra.com), *Doing Business* database.

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## What can development agencies do

If we were at the Oscars, development institutions would take a best-supporting actor award for several of the reforms described here. The large improvements in the business environment in Serbia, Macedonia, El Salvador, Guatemala were helped by the advice and attention of either the World Bank, the USAID, the MCA, or a bilateral agency like Sweden's SIDA.

For example, in 2004 donors included a reform of business registration in the list of 10 priorities for the new Serbian government. The Swedish International Development Agency was the biggest supporter of the reform. The World Bank and USAID commissioned several consulting studies, and Microsoft Corporation provided software installation expertise. The total cost of reform was about €2 million (\$2.3 million). The registry is now fully self-financing.

As another example, in November 2005 the Ministry of Finance of Mexico made an all-out effort to shepherd a new securities law through Congress. But opponents offered amendments that would affect 4 key provisions of the bill—amendments that would eviscerate the law's small investor protections. To help make the case for reform, Finance Minister Diaz asked the World Bank's *Doing Business* team to use its "protecting investors" indicators and benchmark the draft proposed by the government against the existing law and against the watered-down alternative proposed by a prominent tycoon.

The results were striking. Under the existing law, Mexico ranked 125 of 145 countries measured by the *Doing Business* investor protection index, with some of the weakest protections in the world for minority shareholders. Among Latin American countries measured, only Honduras and Venezuela had weaker investor protection.

If Mexico passed the law as presented by the Ministry of Finance, Mexico would shoot up the ranking index 92 places—to 33. Under the alternative law, Mexico's rank would have fallen to 132. "The simulations stirred enormous interest in Congress and in the media by showing the dramatic differences in Mexico's business environment if the law were not adopted," says one Ministry of Finance official. "If approved as proposed by the government, the new law would enhance investor protection and foster investment in publicly traded and even privately held companies. But if the changes proposed by the outside group were accepted, the opposite would happen."

Money sometimes helps: to finance new computers and refurbish courts or more generally provide the government with space to "buy out" opponents of reforms. But most reforms to business regulation aren't expensive. The Serbian business start-up reforms cost €2 million. Transforming Macedonia's labor laws cost only the time of legal drafters. El Salvadorian reformers spent only \$90,000. Instead, donors help by bringing in relevant experience from other countries and by keeping the political determination of the government unwavering.



Perhaps the biggest contribution development agencies can make is to benchmark reform progress. Publishing comparative data on the ease of doing business inspires governments to reform. Since its start in October 2003, the *Doing Business* project has inspired or informed 86 reforms around the world. Mozambique is reforming several aspects of its business environment, with the goal of reaching the top rank on the ease of doing business in southern Africa. Burkina Faso, Mali and Niger are competing for the top rank in West Africa. Georgia has targeted the top 25 list and uses *Doing Business* indicators as benchmarks of its progress. Mauritius and Saudi Arabia have targeted the top 10.

Comparisons among states or cities within a country are even stronger drivers of reform. Recent studies across 13 cities in Brazil and 12 in Mexico have created fierce competition to build the best business environment. The reason is simple: with identical federal regulations, mayors have difficulty explaining why it takes longer or costs more to start a business or register property in their city. There are no excuses.

To be useful for reformers, indicators need to be simple, easy to replicate and linked to specific policy changes. Only then will they motivate reform and be useful in evaluating its success. Few such measures exist. But this is changing. In several countries, such as Mali and Mozambique, private businesses now participate in identifying the most needed reforms. Used to bottom lines, they bring a renewed focus on measurement. The culture of bureaucrats telling bureaucrats what's good for business is disappearing. Going with it is the aversion to measuring the results of regulatory reforms.