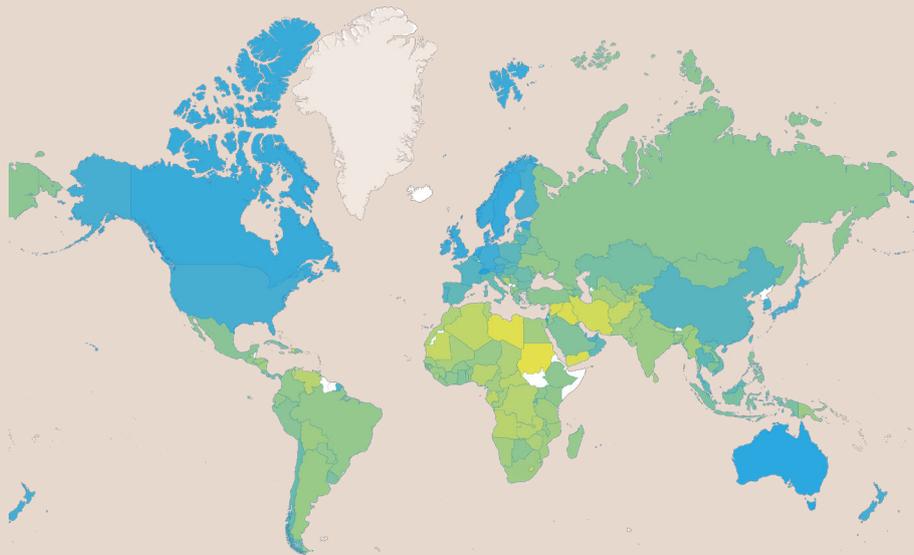


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# ELITE QUALITY REPORT 2022

## Crony capitalism and the importance of context

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## Crony capitalism and the importance of context

*Crony capitalism* (CRO, i.2) is an Indicator based on a notion developed by Gandhi and Walton (2012) that measures the wealth accumulated by a nation's billionaires (closely associated with the government) from economic rent seeking activities—in industries such as energy, real estate or banking—that are classified as “crony”. The Crony Capitalism Index, an attempt to measure such activities by *The Economist* was published in 2014 and 2016, but then discontinued. Most scholars have argued that the costs of crony capitalism are substantially higher than any benefits. Nevertheless, depending on the context, crony capitalism might be judged differently. In this piece I will examine the economies of the Hong Kong Special Administrative Region (HKSAR), China, and Singapore to explore what these differences might be.

Notwithstanding its simplicity, the CRO is an illuminating Indicator that illustrates the power of elites or special interest groups (SIGs) in a political economy, since dominance in ‘crony’ industries entails Regulatory Capture (i.2). The agency of crony elites might result in adverse effects such as wealth inequality, social immobility, and lower incentives for value creation. For example, Malaysia (CRO, i.2, rank # 53), the Philippines (CRO, i.2, rank # 43), and Ukraine (CRO, i.2, rank # 44) all display these problems to a certain degree.

Counterintuitively, the correlation between CRO and *Political corruption* (COR, i.1) is rather insignificant considering the underlying interconnectedness between politics and cronyism. Nonetheless, it could be misleading to conclude that there is no relationship between the two as it is possible that both crony capitalism and political corruption could be covert and not well-documented (see *The Economist's* comments on China below, for example). Failure to document the existence or extent of cronyism or political corruption might further imply that there is overwhelming Political Power that could potentially be value extractive.

Some scholars therefore propose that crony capitalists and powerful elites be reduced, and their agency minimized. Enderwick (2005) suggested that the enduring recession in Japan was consequential of its inability to reform its crony system and contrasted it with the success of the US system that gained worldwide competitiveness through the amelioration of cronyism in the 1980s and 1990s. Breakfast and Madumi's (2020) case study on South Africa further established the urgent need to reduce cronyism to consolidate social stability and facilitate economic growth. However, others see it differently: in certain contexts, elites might be a force for value creation. In fact, some scholars have argued that prosperity in terms of economic growth and social stability has been created as a result of crony capitalism. Rubin (2016) identified the possibility of an efficient type of crony capitalism following the logic of the “theory of the second best” which suggests that such activities might deliver market efficiencies, as demonstrated by the banking bailout and Medicare in the US, in which the former prevented or cushioned the undesirable impacts of an economic recession, whereas the latter cut research and development (R&D) costs and accelerated R&D progress. Glynn (2020) takes this idea a step further and posits that a non-competitive market led by crony capitalism might enhance social welfare in certain economies. Examples that may support this assertion include the HKSAR, China and Singapore.

Given its extraordinarily high property prices and lax anti-trust regulations, HKSAR ranked # 1 in the original Crony Capitalism Index published in 2014. Elites in the HKSAR range from property developers to bankers, and are undeniably the target of the ire of disgruntled citizens. At the same time, they have indisputably created value within an economy that has a consistently low unemployment rate, and has realized extensive success in globalization having achieved an internationally significant status. Perhaps crony capitalism in HKSAR is causing dissatisfaction, but it has also contributed to prosperity for decades. Cronyism has, and is likely to continue to be, an indispensable part of the HKSAR economic model.

We now turn our attention to the authoritarian capitalistic economies of China (CRO, i.2, rank # 34) and Singapore (CRO, i.2, rank # 59). Although China did not rank badly in the original 2014 Crony Capitalism Index, The Economist commented on its crony features:

*“...recent exposés suggest that many powerful politicians have disguised their fortunes by persuading friends and family to hold wealth on their behalf. Unreliable property records also help to disguise who owns what...China’s billionaires, in whatever industry, are often chummy with politicians and get subsidised credit from state banks...”*

Yet for China, as well as Singapore, it could be argued that crony elites also produce spectacular economic and political value. China and Singapore both have very high Political

Value (iii, rank # 9, and iii, rank # 1, respectively) and Economic Value (iv, rank # 32, and iv, rank # 1, respectively) rankings. Neither state is extractive, thus under the right leadership, cronyism might organize the economy around the principle of value creation, either directly through state-owned enterprises or indirectly through crony business elites. That is, an authoritarian state might be able to manage cronyism better than a democratic state on the basis of political elites balancing business interests.

All in all, the CRO provides an overview of the severity of an economy’s exposure to cronyism. However, the notion is ambiguous and as suggested above requires further interpretation to ascertain whether cronyism is value extracting or creating, given that the political context and economic system moderate its impact.

Hung Zhen Feng, Johnson

**Visual 4.2:** EQx Scores correlation with Political corruption (COR, i.1)

Note: Orange dashed line indicates a fitted regression line. Adjusted R-squared: 0.519.  
Random selection of country codes are printed in case of country overlaps.  
Points are coloured according to overall EQx performance.

