

James Surowiecki in the New Yorker

Whatever happens on the ice and snow of Sochi in the next couple of weeks, one thing is certain: this Winter Olympics is the greatest financial boondoggle in the history of the Games.

Back in 2007, Vladimir Putin said that Russia would spend twelve billion dollars on the Games. The actual amount is more than fifty billion. (By comparison, Vancouver's Games, in 2010, cost seven billion dollars.) Exhaustive investigations by the opposition figures Boris Nemtsov, Leonid Martynyuk, and Alexei Navalny reveal dubious cost overruns and outright embezzlement. And all this lavish spending (largely paid for by Russian taxpayers) has been, as Nemtsov and Martynyuk write, "controlled largely by businesspeople and companies close to Putin."

Sochi is emblematic of Russia's economy: conflicts of interest and cronyism are endemic. But the link between corruption and construction is a problem across the globe. Transparency International has long cited the construction industry as the world's most corrupt, pointing to the prevalence of bribery, bid rigging, and bill padding. And, while the sheer scale of graft in Sochi is unusual, the practice of politicians using construction contracts to line their pockets and dole out favors isn't. In the past year alone, Quebec learned about systematic kickbacks and Mob influence in the awarding of city construction contracts. In Turkey, Prime Minister Recep Tayyip Erdoğan has become embroiled in a vast scandal involving friendly construction tycoons who were given cheap loans and no-bid contracts. And a recent report from the accounting firm Grant Thornton

estimated that, by 2025, the cost of fraud in the industry worldwide will have reached \$1.5 trillion.

What makes construction so prone to shady dealings? One reason is simply that governments are such huge players in the industry. Not only are they the biggest spenders on infrastructure; even private projects require government approvals, permits, worksite inspections, and the like. The more rules you have, and the more people enforcing them, the more opportunities there are for corruption. And, in many countries, the process of awarding contracts and permits is opaque. As Erik Lioy, a forensic accountant and fraud expert at Grant Thornton, told me, “When it’s not clear how projects get approved, people assume the worst, and that provides incentives to do a bribe or kickback.”

On big government projects, additional factors kick in. Such projects are rare, and construction work is erratic, so politicians with contracts to award have immense leverage. For contractors, bribery will always be attractive, because the cost of a bribe is dwarfed by the value of a contract—an effect known to economists as the Tullock paradox. And, as a study by Neill Stansbury, the co-founder of the Global Infrastructure Anti-Corruption Centre, put it, when a project is really big “it is easier to hide large bribes.” Then, too, Lioy explains, “most big projects involve building something unique, or at least something that’s never been built in that place before, and that makes it harder to estimate if costs are reasonable.” Corruption is obvious only when costs are completely absurd—which Nemtsov and Martynyuk have shown is the case with Sochi’s ice arenas and ski jumps.

Sochi is a monument to Putin’s Russia—a nationalist

showcase, intended to demonstrate just how far the country has come in the past two decades. It has also given Russia its first world-class winter resort, and has significantly developed the infrastructure of the Caucasus. In that context, overspending can become, perversely, a point of pride. The contractors on the Pyramids almost certainly padded the bills, too.

It's no surprise that graft-ridden grandiose projects are most common in countries where government isn't accountable. But even politicians who (unlike Putin) have to worry about being reelected often see benefits in unnecessary or wasteful construction spending, because it gives the economy a short-term boost. Turkey's construction spree, for instance, has played a major role in its economic boom. Construction creates jobs, and often reasonably well-paying ones. That's why, going back to the days of Boss Tweed, pouring money into construction projects has been a key part of what's sometimes known as "populist clientelism"—a system that allows politicians both to reward cronies and to appeal to voters.

But an economic boost based on corrupt spending is an illusion, the equivalent of a sugar high. Paolo Mauro, an economist at the I.M.F., says simply, "Corruption is bad for economic growth." It's well documented that corruption discourages investment, because it makes businesses uncertain about what it takes to get ahead; as one study put it, "Arbitrariness kills." Corruption also skews government spending. The economists Vito Tanzi and Hamid Davoodi found that corruption leads politicians to overinvest in low-quality infrastructure projects while skimping on maintaining existing projects. (It's easier to collect bribes on new construction than on maintenance.) And, in a pathbreaking study nearly twenty

years ago, Mauro found that countries with high levels of corruption spent little on education. In economist-speak, corrupt politicians put too much money into physical capital and not enough into human capital. Crony construction capitalism leaves us with too few teachers and too many ski jumps to nowhere. ♦