World Development Vol. 36, No. 10, pp. 1692–1708, 2008
© 2008 Elsevier Ltd. All rights reserved
0305-750X/$ - see front matter
ELSEVIER
www.elsevier.com/locate/worlddev
doi:10.1016/j.worlddev.2007.10.012

# World Bank Conditional Loans and Private Investment in Recipient Countries

MARIAROSARIA AGOSTINO *
*University of Calabria, Arcavacata di Rende (CS), Italy*

**Summary.** — World Bank conditional loans might affect private investment in recipient countries not only through the funds they provide, but also via the policy conditions they include and the transfer of knowledge they imply. This work investigates the impact of these channels on private investment, considering also the particular effect of the formal commitment to reform, which necessarily comes along with conditionality. Taking into account the selection problem posed by participation in World Bank programs, the results indicate that backed commitments are associated with lower investment ratios in the short-run, and none of the other potential channels of influence seem to counterbalance this negative impact.
© 2008 Elsevier Ltd. All rights reserved.

*Key words* — World Bank, conditional loans, private investment, commitment to reform, non-random selection

## 1. INTRODUCTION

World Bank and IMF conditional loans are designed to support policy and institutional reforms in developing countries. Therefore, the governments that sign this kind of loans have to commit themselves to implementing certain policy menus of reforms before they will actually receive the funds agreed to. The question of whether in the past two decades the conditional aid provided by these two institutions has fostered sustainable reforms, and promoted economic development is still controversial. In fact, policy-based lending presents a mixed record (see World Bank, 1998), and its real impact is difficult to assess for two main reasons. First, it is difficult to separate the economic effects of the loans from the effects of other observable and unobservable circumstances that brought the country to ask assistance. In addition, conditional loans may affect the economic performance of recipient countries through several channels, such as the amount of funds they provide, the policy conditions they include, and the transfer of knowledge and advice that they imply.

This paper aims at investigating the effect of World Bank Structural (and Sector) Adjustment Loans on private investment, by distinguishing the channels aforementioned and by controlling for the fact that the countries receiving loans are a non-random sample of all possible countries. By doing so, this work combines the features of two recent strands of the literature on the subject: one, which emphasizes the importance of disentangling the impact of different channels through which IMF and World Bank programs may influence macroeconomic outcomes (see Bookmann & Dreher, 2003; Dreher, 2004), and another that advocates the use of appropriate econometric techniques in order to account for the potential selection bias implicit in participation

* This paper was partially written during my visit to the Department of Economics, University of Aarhus. Their hospitality is gratefully acknowledged. An earlier version was presented at the "Research on the World Bank" workshop, Central European University, Budapest, April 2nd 2005. Special thanks go to Jesper Bagger and the workshop participants for their discussion and useful suggestions. I am also indebted to three dedicated referees, whose precious observations reshaped the original manuscript. Finally, I am grateful to Damiano Silipo and Francesco Aiello for their comments. Any errors are solely my responsibility. Final revision accepted: October 3, 2007.

in structural programs (see Przeworski & Vreeland, 2000; Vreeland, 2003).

Differently from most previous studies, which focus their analysis on the long-term impacts, this work adopts a short-run perspective. This time horizon is considered given the crucial role that the investment response can play not only in the long term for the economic growth, but also in the short term for the survival of the reforms themselves. Considering only the long-term investment response, by appealing to the difficult economic conditions characterizing new recipient countries, implies neglecting an important aspect: a short-run investment response is highly desirable, as it may make the adjustment effort socially more acceptable and increase the probability that the reforms will be maintained. Indeed, for a Structural Adjustment Program (SAP) to survive, it is extremely important that good effects are quickly visible, as negative effects tend to prevail: packages usually include harsh economic reforms involving budget cuts, privatization, and labor "flexibility," which are likely to increase unemployment in the short run. Additionally, given the intense cooperation between the two institutions, frequently Bank loans have been coordinated with stabilization programs administered by the Fund. Hence, if a positive investment response materializes in the short-run, this is likely to smooth the progress also of the Fund's targets.

Considering a short time horizon allows also the assessment of which of the mentioned channels exerts a prompt influence, and therefore might be considered to be key determinants of how long the program will endure. Focus is particularly on the potential short-term role of the formal commitment to reform, which necessarily comes along with conditionality and may represent a signal that the governments send to private investors in order to boost their investment response.

To shed light on these issues, a sample of both recipient and non-recipient countries is employed, and the impact of SAPs on investment is assessed by using a methodology that accounts for the selection problem posed by participation in World Bank programs, by allowing the investment and the selection processes to be potentially correlated. In particular, the first process is modeled as an empirical investment equation for developing countries, while the second is modeled following the recent literature on the IMF and World Bank loans determinants (see, among others, Abouharb & Cingranelli, 2005; Knight & Santaella, 1997; Vreeland, 2003).

The main finding of this paper is that backed commitments to reform appear associated with lower investment ratios, and none of the other potential channels of influence seem to counterbalance this negative impact.

The remainder of the paper is organized as follows: the next section reviews the literature on the impact of adjustment programs on economic outcomes. After a brief description of the traditional approaches used to analyze the Bank programs effects, Section 2 focuses on the two strands of the literature that guide the empirical analysis. Section 3 describes the empirical question and the methodology employed. Furthermore, it illustrates the theoretical assumptions underlying the adoption of the estimated equations, with the definition and justification of each variable. Section 4 presents the data, describes the results obtained, and reports the robustness checks performed. Section 5 is a conclusion.

## 2. LITERATURE REVIEW: SAPS EFFECTS

A large number of studies have analyzed the economic and social consequences of World Bank programs on recipient countries (for a detailed review of this literature see Abouharb & Cingranelli, 2005). Most of them concern single case studies or small-*n* comparisons, and adopt two main methodological approaches: the before–after and/or the with–without approach.

The before–after approach compares macroeconomic variables before and after the implementation of SAPs (see e.g., Andriamananjara & Nash, 1997). Any differences discovered are attributed to the programs. An evident weakness of this method is that it does not distinguish between the influence of SAPs and that of other factors, which may affect macroeconomic outcomes over time. Indeed, the implicit assumption is that non-program determinants of macroeconomic performance are constant over time.

The second approach compares adjusting and non-adjusting countries by employing matching pairs of countries or, more generally, a "treated" and a "control" (non-treated) group of countries (see, for instance, Harrigan & Mosley, 1991). In an ideal setting, for each adjusting country there should be at least another non-adjusting country experiencing exactly the same political and economic circumstances. As this

دریافت فوری ← متن کامل مقاله

ISIArticles
مرجع مقالات تخصصی ایران

- ✓ امکان دانلود نسخه تمام متن مقالات انگلیسی
- ✓ امکان دانلود نسخه ترجمه شده مقالات
- ✓ پذیرش سفارش ترجمه تخصصی
- ✓ امکان جستجو در آرشیو جامعی از صدها موضوع و هزاران مقاله
- ✓ امکان دانلود رایگان ۲ صفحه اول هر مقاله
- ✓ امکان پرداخت اینترنتی با کلیه کارت های عضو شتاب
- ✓ دانلود فوری مقاله پس از پرداخت آنلاین
- ✓ پشتیبانی کامل خرید با بهره مندی از سیستم هوشمند رهگیری سفارشات