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What did structural adjustment adjust? The association of policies and growth with repeated IMF and World Bank adjustment loans

William Easterly*

269 Mercer Street, 7th floor, New York University, New York NY 10003, United States

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Abstract

Analysis of adjustment loans often overlooks their repetition to the same country. Repetition changes the nature of the selection problem. None of the top 20 recipients of repeated adjustment lending over 1980–99 were able to achieve reasonable growth and contain all policy distortions. About half of the adjustment loan recipients show severe macroeconomic distortions regardless of cumulative adjustment loans. Probit regressions for an extreme macroeconomic imbalance indicator and its components fail to show robust effects of adjustment lending or time spent under IMF programs. An instrumental variables regression for estimating the causal effect of repeated adjustment lending on policies fails to show any positive effect on policies or growth.

JEL classification: E6; F4; O1; O4
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1. Introduction

On February 5, 1980, World Bank President Robert McNamara sought and received approval from the World Bank Board to launch a new instrument: the structural adjustment

* Tel.: +1 212 992 8684.
E-mail address: William.Easterly@NYU.edu.

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loan (SAL). The proposal followed a year of discussion with the operations chief Ernest Stern, with the outline of the SAL emerging on a flight the two took together to the Bank-Fund Annual Meeting in Belgrade in late September 1979. The loans would provide finance over a period of several years in return for reforms in trade protection and price incentives for efficient resource use.[1] The introduction of the new instrument came against the backdrop of the second oil shock in 1979. It was intended as a preventative instrument so that the "current account deficits of many developing countries do not become so large as to jeopardize seriously the implementation of current investment programs." Although the IMF had always been making "adjustment loans" in the form of standbys, the IMF also in the 1980s expanded the number and maturity of adjustment loans it was making.

The dual rationale from the SALs from the beginning was to maintain growth and to facilitate balance of payments adjustment. The "specific objective" of the SALs were to help countries "reduce their current account deficit to more manageable proportions by supporting programs of adjustment ... to strengthen their balance of payments, while maintaining their growth and developmental momentum."[2] As the 1981 World Development Report said, successful adjustment implies "a minimum sacrifice of income growth."[3] This emphasis on growth continued. In June 1983, for example, the World Bank and IMF published excerpts of speeches by their respective heads under the overall heading: "Adjustment and growth: how the Fund and the Bank are responding to current difficulties."[4] In 1986, the World Bank president A.W. Clausen gave a speech entitled "Adjustment with growth in the developing world: a challenge for the international community".[5] In 1987, the World Bank and IMF published a volume entitled "Growth-oriented adjustment programs" with an introduction discussing the "fundamental complementarity" of "adjustment and economic growth."[6]

Because the SALs were supposed to facilitate balance of payments correction, the structural adjustment loans were intended to end after a period of several years of adjustment. As the initial McNamara document put it, structural adjustment lending entailed "an association with a borrower in a program of structural change over 3 to 5 years which will require financial support."[7]

A flavor of the early structural adjustment package is given in 1981 in the first of what would turn out to be 26 structural adjustment loans to Cote d'Ivoire:

> The loan would be in support of the Government's program of structural adjustment. The reforms envisaged by the program are designed to improve the level of public savings and the efficiency in the use of public resources; restructure the agricultural planning system and associated development institutions so that an expanded, well-designed investment program yielding high returns can be mounted in the sector;

[1] Kapur et al. (1997), volume I, p. 509.

[2] World Bank (1980), pp. 67–68.

[3] World Bank (1981a,b), p. 4.

[4] World Bank and IMF "Adjustment and growth; how the Fund and Bank are responding to current difficulties." 1983.

[5] Clausen (1986).

[6] Corbo et al. (1987).

[7] Kapur et al. (1997), p. 510.