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Has Policy-Based Lending by the IMF and World Bank Been Effective in the Arab World?

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The benefits of policy-based lending have been hotly debated in development circles in recent years. However, little research has focused on countries in the Arab world. This Development Viewpoint provides a brief assessment of the effects of such lending by the IMF and World Bank in four typical countries in the Middle East and North Africa—Egypt, Jordan, Morocco and Tunisia (see Harrigan and El-Said (forthcoming 2008)).

All four countries have received extensive lending based on adopting programmes of stabilisation and structural adjustment. But this Development Viewpoint questions whether such lending has helped generate self-sustaining growth—namely, the type of growth needed to address the region's pressing socio-economic problems (see table).

Growth and Aid in the Case-Study Countries

Country	GDP per capita Annual Growth Rate 1990-2005	Average Annual Aid per capita 1986-2004, US$
Egypt	2.4	36.8
Jordan	1.6	140.0
Morocco	1.5	24.1
Tunisia	3.3	29.1

Source: *World Development Indicators* and *Human Development Report* 2007/08

The four countries in question have often been held up as successful economic reformers. But IMF and World Bank lending to the four has been governed as much by geo-political considerations as the need for economic reforms. Lending has often responded to such political factors as a regime's shift towards a pro-Western foreign policy, peace overtures to Israel or opposition to the rise of Islamic fundamentalism.

This mixture of motives partly explains why the reform programmes of these countries have generated, for the most part, only spurts of economic growth, but not a brisk sustainable pattern of employment-generating growth.

Stabilisation without Adjustment

Though the four countries embarked on economic reform programmes at different times during the 1980s and 1990s, they shared common characteristics at the beginning of reforms: high levels of unsustainable debt, low foreign-exchange reserves, large fiscal and current-account deficits and undiversified economies. Tunisia was exceptional in having achieved a significant measure of economic diversification before its economic reforms.

IMF-supported stabilisation programmes were relatively successful in three of the four countries. Jordan had difficulties with stabilisation because the IMF and World Bank pushed for early and rapid liberalisation. Moreover, Egypt and Morocco failed to make progress on structural adjustment partly because the stabilisation objectives imposed by the IMF overwhelmed efforts to strengthen the supply side of their economies.

In all four countries public investment was cut sharply because stabilisation programmes were fixated on reducing fiscal deficits. In Morocco, for instance, such investment plummeted from 13 per cent of GDP in 1982 to only four per cent in 1986.

Such cuts served only to undermine efforts to use structural adjustment to build up the supply side of these economies, which could have laid the basis for sustainable growth. Part of the motivation was a prevailing ideology that favoured a 'minimal state' and believed that public investment would crowd out private investment.

A Lack of Sustainable Growth

The growth process generated by structural adjustment in these four countries rested on weak foundations: it tended to be extensive (based on factor accumulation) rather than intensive (based on productivity gains) even though adjustment was touted as a way to foster greater efficiency throughout an economy.

Favourable external factors often played an important role in stimulating growth. For instance, Morocco's boom in the late 1980s was fuelled mostly by large aid inflows, debt relief and low oil import prices. Egypt's growth in the early 1990s was attributable to huge influxes of foreign aid and massive debt forgiveness.

While structural adjustment programmes favoured export-led growth, most of the growth attained by these countries was generated by domestic demand. This was usually concentrated in the non-tradable sectors, such as construction and real estate. And booms were linked to an appreciation of the exchange rate based on significant inflows of capital, such as ODA or remittances.

In many respects, Tunisia's sustainable growth was an exception: it was more export-led and based on greater economic diversification. A strong developmental state, which implemented heterodox policies, had already carried out substantial structural transformation of the economy well before economic reforms. It implemented an active industrial policy, maintained price controls on key productive inputs and provided trade protection for domestic industry.

In contrast, the liberal economic reforms introduced in the other countries by the IMF and World Bank, though having some positive effects, essentially failed to lay a sound foundation for sustainable economic progress. Growth was sporadic and low on average—heavily dependent on artificial factors such as booms in non-tradable sectors or transitory factors such as favourable external conditions.

More recently, growth has increased in some Arab economies, but this is less likely the dividend of the reform process than another spurt of unsustainable growth based on temporarily favourable external factors.

References:
Harrigan, Jane and El-Said, Hamed (forthcoming 2008). *Aid and Power in the Arab World*. Palgrave Macmillan.