

Contributions to Economics

Omer Javed

# The Economic Impact of International Monetary Fund Programmes

Institutional Quality, Macroeconomic Stabilization and Economic Growth



Springer

# **Contributions to Economics**

More information about this series at <http://www.springer.com/series/1262>

Omer Javed

# The Economic Impact of International Monetary Fund Programmes

Institutional Quality, Macroeconomic  
Stabilization and Economic Growth



Springer

Omer Javed  
Lahore, Pakistan

ISSN 1431-1933 ISSN 2197-7178 (electronic)  
Contributions to Economics  
ISBN 978-3-319-29177-2 ISBN 978-3-319-29178-9 (eBook)  
DOI 10.1007/978-3-319-29178-9

Library of Congress Control Number: 2016934927

Springer Cham Heidelberg New York Dordrecht London  
© Springer International Publishing Switzerland 2016

This work is subject to copyright. All rights are reserved by the Publisher, whether the whole or part of the material is concerned, specifically the rights of translation, reprinting, reuse of illustrations, recitation, broadcasting, reproduction on microfilms or in any other physical way, and transmission or information storage and retrieval, electronic adaptation, computer software, or by similar or dissimilar methodology now known or hereafter developed.

The use of general descriptive names, registered names, trademarks, service marks, etc. in this publication does not imply, even in the absence of a specific statement, that such names are exempt from the relevant protective laws and regulations and therefore free for general use.

The publisher, the authors and the editors are safe to assume that the advice and information in this book are believed to be true and accurate at the date of publication. Neither the publisher nor the authors or the editors give a warranty, express or implied, with respect to the material contained herein or for any errors or omissions that may have been made.

Printed on acid-free paper

Springer International Publishing AG Switzerland is part of Springer Science+Business Media (www.springer.com)

*To the pursuit of knowledge for bringing  
welfare*



# Foreword

Institutions are important to understand the economic growth and to explain their quality. The most relevant empirical studies of Acemoglu, Robinson, and Rodrik demonstrate this evidence and demonstrate an open field of research in this direction. This book deals with a range of topics that are important for both academics and policymakers alike and emphasizes that usefulness of economics is enhanced when orthodox thinking is augmented with the underlying heterodox assumptions of Institutional Economics, whereby (among revisiting other Neo-Classical assumptions) the existence of transaction costs is not only understood to be non-zero, feeding in turn into production costs, but where market, hybrid, and firm structures are all seen to be competing frameworks for reaching at minimized transaction costs. The book, making an applied research under this premise, has made a significant contribution in putting up a strong case for the IMF (International Monetary Fund) to mainstream institutional focus in its programmes and to revise the underlying Neo-Classical assumptions of its programmes in the light of Institutional Economics.

When the author first approached me in early 2012, with a request to supervise his research to explore the consequences of greater institutional focus on the performance of IMF programmes, given my long-term interest in political economy, heterodox economics, and public economics, I found a natural inclination to be a part of this exciting research project. Reasons for doing this were manifold, which made all the more sense as the research progressed during the course of the PhD in Economics programme.

Firstly, research literature during the last few decades had been emphasizing a policy framework based on deeper institutional fundamentals. Secondly, resurgence of Institutional Economics as a mainstream economic discipline since the 1980s brought centre stage the positive consequence of institutions for economic growth for countries in general, but this development could not find much attention and focus in IMF programmes. This situation presented itself as an important ‘missing link’ in the wake of neutral impacts of IMF programme conditionalities on economic growth in recipient countries and therefore appeared to be a significant



and relevant motivation behind the research project. Lastly, and more importantly, the author being a former economist at IMF's office in Pakistan (where he worked for some years before starting the PhD programme) showed relevant first-hand exposure to the nature, working, and evolution of IMF programmes and, therefore, reflected the much needed appropriate mix of relevant professional experience and sound economic knowledge (for example, his master's degree in Economics earlier from the University of York, United Kingdom). Subsequently, the doctoral thesis that came about was received exceedingly well by external evaluators and PhD defence examiners.

The book at hand is an amended form of the PhD thesis in Economics, whereby primarily a full section has been included in Chap. 4, which analyses the institutional situation in Pakistan from the perspective of Institutional Economics. Taking a large dataset of political and economic institutional variables from new Institutional Economics literature, for a panel of IMF member countries, in terms of subgroups as non-programme and programme countries, along with frequent or prolonged users of IMF resources, over three decades (1980–2009), the study explores the nature of role and relationship between significant institutional determinants and macroeconomic stability, and economic growth, while also illustrating it with the example of a frequent user in the shape of Pakistan. This research holds important results. It finds the consequence of improvement in institutional quality determinants to be positive for macroeconomic stability and economic growth in IMF programme countries. This makes the book an important read for economic policymakers and academicians in general and the ones working on IMF programmes in particular (in terms of both IMF staff and related country authorities). The results of this applied research, it is hoped, will help improve IMF programmes in terms of providing a greater understanding to formulate current and future programmes that are more cognizant of enhancing institutional determinants.

The book also puts focus on the prolonged users of IMF resources. Moreover, it illustrates this by making a counterfactual analysis in the shape of enhanced institutional focus of IMF programmes on the stability and growth of Pakistan. Overall, the book is quite timely as the world embarks on achieving Sustainable Development Goals agreed upon at United Nations last month, since a considerable number of developing countries are either programme countries or prolonged users of IMF resources, and policy recommendations of this book will provide useful prescriptions and food for thought for development economists and policymakers in reaching at context-specific targeted interventions to channelize the improving-institutions-causing positive consequences on macroeconomic stability and economic growth, for reducing poverty and laying stronger basis for sustained development.

Department of Economic Policy and World Economic Structure      Rosa Nonell  
Faculty of Economics and Business  
University of Barcelona  
Barcelona, Spain  
October 25, 2015

# Preface

This study is motivated by the overall poor performance of International Monetary Fund (IMF) programmes in recipient countries in terms of economic growth consequences and tries to explore the relevance of institutional determinants for economic growth in these programme countries. The analysis, at the same time, also takes into consideration the claim by New Institutional Economics (NIE) literature, which points out an overall positive consequence of institutional quality determinants on economic growth for countries in general.

While working at International Monetary Fund's Resident Representative Office in Pakistan (my home country), I got the opportunity to closely witness the working of IMF programmes and how the underlying programme assumptions, other country experience, and the role of country authorities impact their formulation. The issues involved pushed me to think deeply into the specific outcomes from such programmes and also created in me a motivation to analyse research literature on the impact of IMF programmes in general. At the same time, while there was talk about structural reforms in such programmes, coming from a developing country experience I found little mention and emphasis, both among country authorities and by the IMF, on understanding the impact of improvement in institutional quality on economic outcomes. This lack of focus motivated me to explore the link between institutional quality and economic impact of IMF programmes.

More than just academic inquisitiveness, the motivation to take up this project at the PhD level was mainly twofold. Firstly, global financial crisis of the recent past challenged conventional wisdom of Washington Consensus and Neo-Classical/Monetarist thought process. Secondly, fundamental economic issues that allowed Pakistan to experience stability and growth only transitorily, even after being a frequent user of IMF resources for many years, pointed towards deeper analysis, and to see how the situation could have been different if the negotiated IMF conditionalities focused more on improving institutional quality.

It may be pointed here that the major part of the book is my PhD thesis in Economics, titled, 'Essays on institutional quality, macroeconomic stabilization, and economic growth in International Monetary Fund member countries'.

The major inclusion outside of the thesis in this monograph/book is in the shape of institutional analysis of Pakistan from the perspective of NIE. I find this analysis, which required a lot of effort and thinking, to be novel in its own right generally, but particularly in the case of Pakistan. Overall, it is hoped that the book will be useful for policymakers at the IMF and in individual countries, especially developing countries (many of which have remained frequent users of IMF resources) like Pakistan, in revising their policies to make them more context specific and meaningfully understanding the important role institutions play for achieving stability and growth.

# Acknowledgements

The book which is primarily an outcome of my work as PhD student at the University of Barcelona (Spain) is indebted primarily to the patient and profound support of my PhD advisor, Dr. Rosa Nonell. The overall support of the Dean of the Faculty of Economics and Business, Dr. Elisenda Paluzie, the Director of the PhD Programme, Dr. Elisabet Viladecans, and in administrative matters from Mr. Jordi Roca (among others) brought seriousness of purpose and comfort to the overall research environment. Moreover, family and friends provided much needed support at the personal level, especially the birth of my first child, my daughter Roshanay, who brought me immense happiness.



# Contents

<b>1</b>	<b>Introduction . . . . .</b>	<b>1</b>
1.1	The IMF and Its Changing Role . . . . .	1
1.2	IMF Programmes and Their Consequence . . . . .	2
1.3	New Institutional Economics and IMF Programmes . . . . .	3
1.4	Motivation . . . . .	5
	References . . . . .	5
<b>2</b>	<b>Determinants of Institutional Quality: A Case Study of IMF Programme Countries . . . . .</b>	<b>7</b>
2.1	Introduction . . . . .	7
2.2	Literature Review . . . . .	9
2.3	Data and Methodology . . . . .	11
2.3.1	Theoretical Design . . . . .	11
2.3.2	Sample . . . . .	12
2.3.3	Data and Variable Description . . . . .	15
2.3.4	Econometric Methodology . . . . .	17
2.4	Estimation and Results . . . . .	18
2.4.1	Robustness Check . . . . .	28
2.5	Conclusion . . . . .	28
	Appendix . . . . .	29
	References . . . . .	33
<b>3</b>	<b>Institutional Quality, Macroeconomic Stabilization and Economic Growth: A Case Study of IMF Programme Countries . . . . .</b>	<b>37</b>
3.1	Introduction . . . . .	37
3.2	Literature Review . . . . .	38
3.3	Data and Methodology . . . . .	41
3.3.1	Theoretical Design . . . . .	41
3.3.2	Sample . . . . .	42
3.3.3	Data and Variable Description . . . . .	43
3.3.4	Econometric Methodology . . . . .	44

3.4	Estimation and Results . . . . .	46
3.4.1	Robustness Check . . . . .	61
3.5	Conclusion . . . . .	62
	Appendix . . . . .	63
	References . . . . .	70
<b>4</b>	<b>IMF Programmes and Institutional Quality Determinants:</b>	
	<b>Economic Scenarios in Pakistan . . . . .</b>	<b>73</b>
4.1	Introduction . . . . .	73
4.2	Literature Review . . . . .	75
4.3	Institutional Analysis of Pakistan: A NIE Perspective . . . . .	79
4.3.1	Tracing the Political Economy . . . . .	79
4.3.2	Defining the Actors in the Political Economy . . . . .	80
4.3.3	Challenging the Assumptions and Actions of Policy . . . . .	84
4.3.4	Designing an Institutional Incentive Structure for Pakistan . . . . .	94
4.3.5	Towards Optimal Governance Structures . . . . .	99
4.4	Data and Methodology . . . . .	101
4.4.1	Theoretical Design . . . . .	101
4.4.2	Sample . . . . .	103
4.4.3	Data and Variable Description . . . . .	103
4.4.4	Econometric Methodology . . . . .	104
4.5	Estimation and Results . . . . .	107
4.5.1	VAR and Impulse Response Functions of Sub-indices of MII and KOF Index of Globalization . . . . .	107
4.5.2	VAR and Impulse Response Functions of MII, Real GDP and KOF Index of Globalization . . . . .	111
4.5.3	Simulations . . . . .	112
4.6	Conclusion . . . . .	114
	Appendix . . . . .	115
	References . . . . .	119
<b>5</b>	<b>Concluding Remarks . . . . .</b>	<b>121</b>
	References . . . . .	124