Politics of Religiously Motivated Lending: The Case of the Islamic Development Bank

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Abstract: Arab countries have been major donors of development aid outside the Development Assistance Committee (DAC). It is argued that Arab aid is different from DAC aid in that large amount of aid flows go to countries with Muslim population on the idea of Islamic solidarity. Though it is true that religion plays a dominant role in allocation of aid by Arab donors, we argue that Islamic societies are not homogeneous and the influence of rival factions within them, particularly the power politics of Sunni-Shia divide on lending decisions have not been subject to intense scrutiny so far. We fill this gap in the literature by examining the impact of power politics of Sunni-Shia divide on aid allocation by Islamic Development Bank (IsDB). We argue that the major shareholder, namely, Saudi Arabia, a strongly pro-Sunni regime, use its influence at the IsDB to ensure favorable treatment from the bank for Sunni majority populated countries. Using panel data on 56 aid recipient countries from IsDB during 1976–2007 period, we find that Sunni majority populous countries are more likely to be favored. However, an increase in aid allocation to Shia majority populous countries is only conditional upon a higher degree of religious tensions with non-Muslim religious communities. Our results are robust to alternative sample and estimation techniques.

Keywords: Development aid, Arab aid, Islamic Development Bank, Sunni-Shia politics.

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"Fourteen centuries after the death of the prophet (Mohammad), in a region full of destruction, killing, occupation, ignorance and disease, you are telling me about Sunnis and Shiites?"[1]

– Esmail Al Hamami, a 67-year-old Sunni Palestinian refugee in Gaza

1. Introduction

Arab countries, often referred to as emerging donors (see Dreher et al. 2011), have actually been major donors of development aid outside the Development Assistance Committee (DAC) since the 1970s (Shushan and Marcoux 2011). It has often been argued that Arab aid is different from that of DAC donors as large amounts flow into countries with significant Muslim populations on the idea of Islamic solidarity (see Neumayer 2003a, Neumayer 2003b). Although we concede that religion plays a dominant role in allocation of aid by Arab donors, we argue that Islamic societies are not homogeneous and the influence of the power politics of Sunni-Shia divide on lending decisions have so far not been subject to intense scrutiny in the development aid literature. This is the gap we fill in the literature by examining the impact of power politics of Sunni-Shia divide on aid allocation by region's largest development agency, the Islamic Development Bank (IsDB hereafter).

The argument is linked to the notorious criticism the development aid agenda has recently received, supported on the view that the interests of donors shape the direction of lending decisions. A wave of studies highlight the fact that developing countries that are politically aligned to the G7, especially to the US, and with significant trade and investment potential are preferred by DAC donors when choosing where to dispense aid. These studies have shown that geopolitical and commercial interests are particularly important for the US (Wang 1999; Alesina and Dollar 2000; Kuziemko and Werker 2006), that commercial interests are particularly important for Japan (Alesina and Dollar 2000; Tuman and Strand

[1] See: http://www.apnewsarchive.com/2013/Hatred-between-Sunnis--Shiites-abounds-in-Mideast/id-3f07728a9d3844fe9384c481f0edbd28

2006), while particular interests play a minor role for small donors such as Canada, Denmark, Netherlands, Norway and Sweden (Alesina and Dollar 2000; Gates and Hoeffler 2004). Similar patterns have also been identified in multilateral institutions, in which DAC donors are major stakeholders, such as the IMF (Thacker 1999; Oatley and Yackee 2004; Stone 2004; Dreher and Jenser 2007; Dreher et al. 2009a; Dreher et al. 2010), the World Bank (Andersen et al. 2006; Fleck and Kilby 2006; Bresslein and Schmaljohann 2013; Kilby 2013) and the Asian Development Bank (Kilby 2006; Kilby 2011; Lim and Vreeland 2013).

The examination of donor interests on aid allocation by Arab donor agencies and institutions has received, on the other hand, less attention in the literature. The limited number of studies on the subject suggests, as highlighted above, that religion and Arab solidarity are the main drivers of Arab aid (Simmons 1981; Hunter 1984; Neumayer 2003a; Neumayer 2003b). In other words, countries with significant Muslim populations are the main beneficiaries of Arab donors. In fact the IsDB was set up in 1973 for this very purpose of providing development assistance to only countries with predominantly Muslim populations. The objective of the Bank is to not only provide financial assistance to Muslim populated countries but also to promote Islam by bundling development aid with the religious aspect (Villanger 2007). This outcome is not surprising when observing the relative neglect of DAC donors in serving Islamic countries compared to other regions worldwide. A back of the envelope calculations show that the Official Development Assistance (ODA) by DAC donors to the Middle East and North Africa (MENA) region represents only 0.7% of the region's GNI, while this same figure is 13% for Sub Saharan Africa, and 3% each for East Asia, Latin America and South Asia respectively (OECD 2010).[2] The disadvantage of Muslim countries in terms of aid received from DAC donors might rely on the fact that the

[2] Note that whatever aid flow which went into this region is concentrated in a handful of countries viz., Iraq which constitutes 47% of total DAC aid flows to the MENA region during the period 2006-2010, and together with Egypt, Morocco, and West Bank and Gaza accounted for more than 80% in the same period (OECD 2010).

group of donors tend to reward democratic and politically allied countries through development assistance, which are not often to find in this side of the world (Alesina and Dollar 2000; Dreher et al. 2009a).

Though it is undeniable that religion plays a dominant role in allocation of aid by Arab donors, Islamic societies are not homogeneous and the influence of internal divisions within them, particularly the power politics of Sunni-Shia divide on lending decisions have not been subject to intense scrutiny. Tensions between Sunni and Shia sects have always polarized Islamic societies, and cooperation as well as confrontation between them is quite evident on various national and international issues. During the Arab spring, Sunni regimes like Jordan and Saudi Arabia came to the rescue of Sunni-led regime in Bahrain to stave off the revolutionary wave of protests backed by the Shia population (Al Jazeera report 2011). On the contrary in Syria, the Iran and Hezbollah supported the Al-Assad Shia regime, while the opposition factions have been openly aided by the Sunni governments of Qatar and Saudi Arabia (Dehghan 2012).

At the forefront of this power politics of the Sunni-Shia divide is Saudi Arabia on one side, which practices *Wahhabism* – an ultra-conservative part of Sunni Islam whose tenets are strongly anti-Shiite, and on the other side is the Shia-dominated 'Axis of resistance' which includes Shia regimes like Iran, Syria and the Hezbollah led coalition (Clark 2012). While Sunnis are the majority across the Islamic world, Shiites have strong majorities in Iran, Iraq, Bahrain and Azerbaijan and form a significant share of the population in Lebanon, Yemen, Syria, Saudi Arabia, Kuwait and other parts in the region (Keath 2013). Though the strife between the Sunnis and Shias could be traced back to the 6th century AD, as the opening quote illustrates, even today ordinary citizens in Muslim countries are exasperated with the power politics of the Sunni-Shia divide. Yet, governments of the Islamic countries have often used sectarian tensions and religion as an instrument of security and foreign policy rather

than focusing on the ways and means to resolve sectarian tensions and promote peaceful relations (see Hunter 2013: 11). In this paper, we examine whether the politics of the Sunni-Shia divide has an impact on how development aid is allocated by the IsDB, the region's largest development bank.

In line with the criticism of major global players pursuing self-interests in their regions of influence through the control of International Financial Institutions (IFIs) in which they hold large stakes, the Saudi-dominated IsDB provides a framework to examine how and to what extent Arab aid allocation is subjected to such political constraints in the context of the Islamic world.[3] The IsDB is not only the largest Arab donor in terms of loans allocated but is also focused exclusively on lending to members of the Organization of the Islamic Conference (OIC), composed of only countries with significant Muslim populations.[4] In this paper, we analyze how sensitive IsDB loan commitments to borrowing members are to the power politics of the Sunni-Shia divide within Islamic society. Using panel data on IsDB loan commitments allocated across its 56 member countries during the 1976-2007 period, we find members with Sunni regimes and large Sunni populations, relative to those with large populations from other Islamic sects and other religions, to be rewarded with significantly more resources from the Bank, as a form of international cooperation from Saudi Arabia. We also observe, however, that members with large populations from other Islamic sects witness increases in development assistance from the IsDB conditional upon the presence of conflicts with other religious groups, such as Christian or Hindus, as these are perceived as common opponents threatening the Islamic solidarity.

[3] Saudia Arabia is the largest stakeholder of the IsDB with 24% of its shares, followed by Lybia with 9%, Iran, Nigera and the United Arab Emirates with 8%, and Qatar, Egypt and Turkey with 7%.

[4] Figures in OFID (2004) suggest that the IsDB is the largest Arab development agency with cumulative loan commitments until 2003 of US$ 34,224 million. Same values for other Arab development agencies are US$ 2,196 million for the Arab Bank for Economic Development in Africa, US$ 15,492 million for the Arab Fund for Economic and Social Development, US$ 238 million for the Arab Gulf Program for United Nations Development Organizations, US$ 6,896 million for the OPEC Fund for International Development, US$ 3,384 million for the Abu Dhabi Fund for Development, US$ 12,400 for the Kuwait Fund for Arab Economic Development, and US$ 6,474 million for the Saudi Fund for Economic Development.

The rest of the paper is organized as follows: Section 2 presents our arguments with anecdotal evidence on how power politics of the Sunni-Shia divide has politicized the aid allocation decisions at the IsDB. Section 3 introduces the data and our estimation strategy. While section 4 presents the discussion on our main results, section 5 conclusions the study**.**

2. The Argument

Founded by OIC in 1973, the IsDB started its operations in 1975, headquartered in Jeddah, Saudi Arabia. The Bank is the leading agency of the Islamic Development Group and membership is restricted to OIC member states. The Bank is composed of 56 members and all of them are eligible to receive loans. The majority of members are geographically located in the MENA region (22 members), however, the membership has been also extended to countries in Sub-Saharan Africa (21 members), Central Asia (6 members), South Asia (3 members), South East Asia (3 members) and Latin America (1 member). The IsDB allocated on average US$ 400 million every year during the period 1976-2007. The resource availability has also been on the rise in the last decade with total loan commitments worth US$ 800 million for the year 2007 (IsDB 2010). These figures place the IsDB as single the largest Arab development agency (IsDB 2010). The major stakeholder of the Bank is Saudi Arabia with 23.6% of the total share capital subscription. Other significant stakeholders include Libya, Iran, Nigeria and the United Arab Emirates, each of them holding around 8% of total share capital of the Bank. It is noteworthy that the voting power of each member representative is linked to the country's contribution to the Bank's ordinary capital stock. The organizational structure of the Bank consists of the Board of Governors, which is the highest policy-making body and delegates its powers to the Board of Executive Directors for the general operation of the Bank. The Board of Governors elects the Chairman of the Bank. All

56 member countries are part of Board of Governors.[5] Each member country has 500 votes plus one vote for every share subscribed. The Board of Governors meets once a year to review the Bank's lending activities and operations, as well as future policies. It is important to note that all the Board decisions are taken by the Board of Governors based on a majority of the voting power represented at the meeting. The Board of Executive Directors, on the other hand, is responsible for the implementation of the policies set by the Board of the Governors. The Board of Executive Directors consists of 18 members in which nine permanent members including Saudi Arabia are the main shareholders, while other nine are elected by the Governors of other countries once in three years. Thus, Saudi Arabia which is the largest stake holder undoubtedly wields great influence on the Board's decisions and policy implementation.

The extensive literature on the allocation of development aid, as noted earlier, emphasizes that aid from DAC donors and multilateral aid institutions is guided by strategic interests (Alesina and Dollar 2000; Kuziemko and Werker 2006; Dreher et al. 2009; Kilby 2009; Hernandez 2013). According to Al-Yahya and Fustier (2011), "fulfilling and maintaining its role as the leader of the Islamic world is a key foreign policy priority of Saudi Arabia." The empirical evidence provided by Neumayer (2003a), in which foreign policy is a key determinant of Arab aid channeled through its various development assistance agencies, indeed corroborates these claims. Moreover, Al-Yahya and Fustier (2011) argues that Saudi Arabia tends to perceive that countries with Islamic affiliated regimes have higher expectations from itself in terms of development cooperation and support. The authors provide examples of numerous requests Saudi Arabia received from the governments of Senegal and Yemen to finance various development projects in their own countries. Several

[5] Each member country is represented on the Board by a Governor and an alternate Governor who are in turn appointed by their respective governments.

other studies present abundant anecdotal as well as empirical evidence to show that religion plays an important role for Arab donors led by Saudi Arabia (Villanger 2007, Neumayer 2003a, Neumayer 2003b, Shushan and Marcoux 2000). In fact, the lending activities of the IsDB are restricted only to the member states of OIC who follow Islamic financing that is compatible with the Shari'ah. Though it is indisputable that religion plays a dominant role in allocation of aid by Arab donors such as Saudi Arabia, it is noteworthy that Islamic societies are not homogeneous. Internal divisions within them, particularly the existing rival tensions and animosity between Sunni and Shia sects have always polarized the Islamic world, and cooperation among these sects as well as confrontation across them is quite evident on national and international matters (Clark 2012).

The power politics of the Sunni-Shia divide could be traced back to the succession battle among Caliphs (Khalifa) around 650 AD. The dispute over succession of Prophet Mohammad in 662 led to schism in the wider Islamic community (Clark 2012). According to Pew Research Centre (2009), Sunnis constitute 80% of the Muslim population while the other fraction is almost entirely composed by Shias. Over the years, Sunni–Shia relations have been marked by fierce conflict, and unsurprisingly sectarian tensions across the MENA region are a common phenomenon (Blanchard 2009). Saudi Arabia, with *Wahhabism* - leading stream of Sunni Islam - as its state religion whose tenets are anti-Shiite, has often been on the forefront to espouse a Sunni united block against the 'Axis of Resistance' led by Shia regimes viz., Iran, Syria and the Hezbollah in Lebanon (Cark 2012). Al-Yahya and Fustier (2011) shows, for example that Saudi Arabia has often accepted the request for development assistance coming from smaller Islamic countries to signal its status as the leader of Islamic world to the Shia-led regimes like Iran. Therefore it is not surprising that Saudi Arabia along with its other Sunni allies as the major stakeholders in IsDB could use its

influence through votes to allocate a higher amount of development aid to Sunni majority populated countries relative to the Shia majority countries.

Anecdotal Evidence

Examples of Saudi Arabia, the major stakeholder, influencing IsDB to allocate development aid based on political considerations are abounding. Focusing on Islamic countries within Sub-Saharan Africa, Ousman (2012) provides evidence that Saudi Arabia has been very open in using IsDB to allocate development aid in education sector to increase school enrolment where African Muslim youth are specially trained at the Salafist and Wahabi education which is based on anti-Shiite tenets. Deegan (1995) provides anecdotal evidence on how Saudi Arabia has used its influence at the IsDB to direct development aid to Sudan. As one example, the Saudi Arabia exerted pressure on Sudan in 1983 to declare its constitution which would enable Sudan to become a Sunni based Islamic state in return for development assistance from IsDB (Deegan 1995). Turning to other examples, Al-Yahya and Fustier (2011) argue that the surge in Saudi Arabia's development aid through various donor agencies to Yemen was largely a response to the armed conflict between the Yemeni government and Shiite rebel groups in the northern region which shares border with the Saudi Kingdom (see Burke 2012). Likewise, Cooper (2007) reports that in a desperate bid to keep the Shia political faction (i.e. Hezbollah-led coalition) from obtaining power in Lebanon, Saudi Arabia used IsDB to allocate development assistance worth US$ 250 million to the newly elected Prime Minister Fouad Siniora from the Sunni faction in 2007.

The Arab Spring, ongoing since late 2010 in several countries of the MENA region, once again brought to fore the intense rivalries between various factions in Islamic societies. For instance, Bahrain, a country whose population is largely Shia but is ruled by a Sunni dynasty (House of Khalifa), has received not only military support from Jordanian and Saudi Arabian Sunni governments to block the revolutionary wave of protests backed by the Shia

population but also received series of development and technical assistance projects from Saudi-led IsDB (Itani 2013). Similarly, to strengthen the Sunni-led Mursi government in Egypt which was reeling under economic crisis, the Saudi Arabian government influenced the IsDB to allocate a higher amount of development assistance after the first foreign trip since taking office by the Egyptian President (Al Arabiya 2012). The uprising in Syria is a counter example: it is a Sunni majority population country presided by a Shia dynasty (Al-Assad family) whose opposition have been internationally aided by the Sunni governments of Qatar and Saudi Arabia, while the ruling family has been assisted by the Iran government, a Shia Islamic Republic, to remain in power (Sanger 2012, DeYoung 2012, Dehghan 2012). Thus, when we consider a Sunni majority populated country's historical experience and then compare it to the experience of other countries, i.e. Shia majority populated countries, we begin to see a pattern. Sunni majority populated countries and Sunni regimes seem to be associated with more IsDB development assistance projects.

We also provide some stylized facts supporting our arguments and the anecdotal evidence on the relationship between religious politics and aid allocation by Saudi-led IsDB. Figure 3 presents a first descriptive look at this relationship. As seen, IsDB member countries with Sunni majority populations received every year on average US$13.2 million by the Bank during the period 1976-2007, surpassing by an important amount members with Shia and other religions majority populations whose same figure is of US$10 and US$7.9 million respectively.

Based on our previous discussion and anecdotal evidence on power politics of Sunni-Shia divide, we thus hypothesize (1): **being a Sunni majority populated country or a Sunni regime increases the probability of receiving higher amount of development aid commitments from IsDB.**

Although the power politics of Sunni-Shia divide is a key determinant of how development aid is allocated by major Arab donors like IsDB, we argue that these internal divisions actually play a less relevant role in the presence of a strong social friction between the Islamic and non-Islamic communities within the recipient member countries.. In fact, Villanger (2007), Mertz and Merts (1983) and Hunter (1984) argue that religious motives, in the name of Islamic solidarity, play an important role while allocating development aid. Neumayer (2003a) estimates that Islamic countries receive a 118% more development aid by Arab donor agencies relative to non-Islamic countries. The Islamic solidarity across different sects is quite evident during conflictive periods with populations of other confessions in multi-religious countries, scenario in which Muslim sects tend to actually form political coalitions to confront their common opponent.

The Lebanese Civil War, lasting from 1975 to 1990, is a notable example to observe the interaction between Sunni and Shia sects under the presence of other religions. Lebanon is a country shared by Christians, Shia and Sunni Muslims, and during the abovementioned conflict both Islamic sects cooperated with each other to confront a common adversary. They both formed the Lebanese National Resistance Front, a militia seeking to overthrow the Christian dominated government. Such examples are not limited to armed resistance alone. Likewise, the foray of the bank's activities in African countries where Muslims form minority group (irrespective of their sect) face hostile relationship with the Christians is an example in offer. Similar such examples can be found in Asia. Robels (2013) reports that IsDB provided US$ 16 million as development assistance to MNLF (Moro National Liberation Front) rebel group which controls Mindanao province in Philippines. The MNLF is a Islamic political organization largely dominated by Shia community was set up in 1969 with the intention to secede Mindanao province from Philippines. MNLF accuses the

Philippines government of economic discrimination against Muslim dominated Mindanao province. Ironically, the MNLF is recognized by the OIC.

Figure 4, in addition supports this evidence. While Sunni and other majority populated members received every year on average larger loans from the IsDB under scenarios of low religious tensions (dark gray bars) relative to those of high tensions (light gray bars) during the 1976-2007 period, exactly the opposite occurs in Shia majority populated members.[6] In the latter cases, members received US$9.7 million in situations of low religious tensions and US$10.7 million in those of high religious tensions, indicating that the IsDB is more likely to back up Islamic sects different to Sunnis under the presence of conflicts with other religions.

We thus test the hypothesis (2) that: **the power politics of the Sunni-Shia divide does not influence aid allocation decisions when conditional upon higher degree of religious tensions with non-Muslim religious communities.**

3. Data and Methods

We analyze a panel dataset consisting of 56 member countries[7] covering the years from 1976 to 2007 (see Appendix 1). The baseline specification estimates the allocation of aid by IsDB to recipient country *i* in year *t*, which is a function of factors capturing donor and recipient interests. Our dependent variable is the amount of aid commitments by IsDB to country *i* in year *t* in US$ (2000 year) constant prices during the 1976-2007 period. Note that our data on aid commitments is plagued with the problem of zeros and missing observations for many countries in the sample. To circumvent this problem, we follow the strategy adopted by Rajan

[6] Note that our measure of religious tensions captures the tensions between Muslim and Non-Muslim population groups within a country. Thus, it is a measure capturing religious tensions but not ethnic tensions between two sects belonging to the same religion.

[7] Note that although the main focus of IsDB is to provide development aid to Islamic republic countries, on occasions, IsDB also allocated development aid to non-Islamic Republics which have significance share of Muslim population.

and Subramanian (2008) to consider average of aid commitments by IsDB during the following periods: 1976-1979; 1980-1983; 1984-1987; 1988-1991; 1992-1995; 1996-1999; 2000-2003; and, 2004-2007. Figure 1 captures evolution of aid commitments by IsDB over the 32 years from 1976 to 2007. As seen, there has been steady increase in aid commitments by IsDB from the mid-1990s onwards. Note that there is a spike during the period of late 1970s which is a result of high oil prices as the largest stakeholders in IsDB namely, Saudi Arabia, Libya, Iran are the world's largest oil producers. As on 2007, IsDB aid commitments are about US$ 900 million. Figure 2 shows mean of aid commitments by IsDB per each member of the Bank. While Qatar and Bangladesh remain the largest recipients of development aid by IsDB, Brunei received least amount of development aid from the Bank.

To test the influence of power politics of Sunni-Shia divide, we introduce four different discrete measures which we group under two categories viz., (i) population based on religious sects and (ii) religious sects of the regime in power. Under the first category we have two variables namely, (a) codes the value 1 if a country is a Sunni majority populated country and 0 otherwise; and (b) takes the value 1 if a country is Shia majority populated and 0 otherwise. We use another dummy variable which takes the value 1 if a country is non-Muslim majority populated and 0 otherwise as our omitted category. Likewise, under religious sects of the regime in power, we use two dummy variables which (a) codes the value 1 if a country is ruled by a Sunni regime and 0 otherwise; (b) codes the value 1 if a country is a Sunni majority populated country and 0 otherwise. Again, we use non-Muslim majority regime as our omitted category. These variables are computed based on the information sourced from the religious population statistics published by the Pew Research Center, as well as on the profiles of the head of states available in in the CIA World Fact book and Encyclopedia Britannica.

In addition, the Shia majority populated dummy and also Shia regime dummy is interacted with the Religious Tension index in order to examine if Bank's preferences towards other Islamic sects are conditional to religious conflicts and frictions with non-Muslim religious communities. The Religious Tension index is sourced from the International Country Risk Guide (ICRG) which takes a minimum value of 0 for cases of high religious tensions and a maximum value of 6 for cases of low or no religious tensions. It is noteworthy that the indicator captures only conflicts and tensions across different religions and not conflicts within Muslim religion.

Concerning the selection of the explanatory variables, we follow the previous literature on aid allocation, in particular that of aid allocation by multilateral agencies (e.g., Kilby 2006, 2011, Neumayer 2003, 2004). We use several variables to examine whether IsDB allocates aid based on the needs of the recipient countries. To reflect needs of recipient countries, we include total population (log) of the recipient country as it is expected that larger countries need more resources to obtain visible effects of aid provision. The other plausible reason for including population is the fact that larger countries on an average tend to receive more aid. Likewise, we use the recipient country's (log) per capita GDP (measured in current prices). We expect a negative effect of this income measure since richer countries need fever aid resources to develop. To account for merit as motive for aid supply, institutional quality in the recipient countries is proxied with a democracy dummy sourced from Cheibub et al. (2010). This measure is based on distinction between regimes in which executive and legislative offices are elected through elections and those in which they are not. Accordingly, the country is coded as democracy (taking the value 1) if elections are contested for executive and legislative offices respectively and 0 otherwise.[8] A civil war dummy is also included, as an ongoing civil war is likely to affect aid allocation by international agencies

[8] For more detailed description and methodology, see Cheibub et al. (2010).

such as IsDB. We include a variable measuring civil war that takes the value 1 if there is armed conflict between an organized group and a state in which at least 25 deaths have occurred in a single year and 0 otherwise (Gleditsch et al. 2002). We also include a measure of trade openness (merchandise trade/GDP) as one of the key aims of IsDB is to provide more aid to countries to promote trade with external world. Finally, as loan demand factors we include a variable measuring the value of the oil production taken from de Soysa (2012). Most of the countries in the Middle East North Africa (MENA) region are oil rich and are expected to depend less on external sources of development assistance. Likewise, we also control for foreign exchange reserves as a share to GDP sourced from World Development Indicators, World Bank 2011. We construct a dummy measure capturing whether a country is experiencing a debt crisis or otherwise based on the information sourced from Laeven and Valencia (2008). Lastly, we control for the bilateral aid allocation by Saudi Arabia (in US$ 2000 constant prices) as a proxy for largest stakeholder's interest in the bank.[9] The details on definitions and data sources are provided in Appendix 2 and the descriptive statistics in Appendix 3.

A distinguishing feature of our dependent variable (i.e., commitment of development aid) is that it has zero observations. The clustering of zero observations is due to the fact that in some country-years the aid commitments by the IsDB was nil. Estimating such models with Ordinary Least Squares (OLS) estimator would violate several assumptions such as a zero mean for the OLS errors thereby resulting in biased estimates (see Neumayer 2002, 2003 for details). This requires a nonlinear method of estimation specification. We adopt a Tobit maximum likelihood estimation procedure with heteroskedasticity consistent robust standard errors (Beck and Katz 1995):

[9] In order to keep Saudi Arabia in the dataset, the value given to this country in a year is the largest bilateral allocation made by Saudi Arabia in that same year.

$$
\begin{aligned}
y_{it} &= \max(0, x_{it}\beta + \delta_{it} + \mu_{it}) \\
\mu_{it} \mid x_{it}, \delta_t &\approx Normal\ (0, \sigma^2_{\mu}) \\
\delta_{it} \mid x_{it} &\approx Normal\ (0, \sigma^2_{\delta})
\end{aligned} \tag{5}
$$

Where, the dependent variable y_{it} is the development aid commitments by the IsDB for recipient country i in year t in US$ 2000 constant prices and x_{it} refers to the aforementioned determinants of aid allocation by the IsDB; δ_t is the time dummies, while μ_{it} is an independently distributed error term assumed to be normal with zero mean and constant variance σ^2. Note that we include country fixed effects only for the specifications containing the interaction terms because our key variables of interest capturing the power politics of Sunni-Shia divide are time invariant. The usage of two-way fixed effects will not only be collinear with time-invariant or largely time-invariant regressors, but will also generate biased estimates (see Beck 2001). It is noteworthy that the β coefficient cannot be interpreted directly in the nonlinear Tobit model. We thus compute the marginal effects of the explanatory variables on either $P(y_{it} > \mid x_{it})$, $E(y_{it} \mid x_{it}, y_{it} > 0)$ or $E(y_{it} \mid x_{it})$. We calculate the marginal effects at the mean of the respective covariates. Note that regression outputs report β coefficients but we refer to marginal effects for the interpretation of the results.

4. Empirical Results

Table 1–3 present our main results. Table 1 show our baseline results in which various measures capturing power politics of Sunni-Shia divide are introduced. More specifically we capture two important measures namely, population based on religious sects and religious sects of the regime in power. Table 2 presents the results of interaction between population based on religious sects and religious tensions. Table 3 presents the results of interaction

between regimes based on religious sects and religious tensions. Before turning to the analysis, we provide some stylized facts on the influence of power politics of Sunni-Shia divide on aid allocation by IsDB. Figure 3 provide a first descriptive look at this relationship. As seen, the Figure shows that major chunk of the development aid from IsDB is allocated to Sunni populated vis-à-vis non-Sunni populated countries. The breakup of aid allocation numbers between Shia and other religious populated countries show that roughly 13 US$ million of the development aid allocated by IsDB goes to Sunni populated countries, while about just under 10 US$ million and eight US$ million of the aid is allocated to Shia and non-Muslim majority populated countries respectively. Similar such conclusions could be derived when we examine the breakup of aid allocation based on religious sects of the regimes. As seen from Figure 4, roughly 40% of the total aid allocated during our study period went to Sunni regime governments while Shia and non-Muslim regimes received roughly 31% and 29% of the IsDB aid respectively. Interestingly, when we split the aid allocation based on the intensity of religious tensions, we find that Shia populated countries receive more development aid from IsDB when faced with higher levels of religious tensions, which is quite the opposite for Sunni populated countries (see Figure 5). While these differences could also be spurious, we turn to the first table which reports the impact of power politics of Sunni-Shia divide on aid allocation by IsDB during 1976-2007 period.

As seen in Table 1, we find that relative to the non-Muslim populated countries, Muslim majority populous countries receive more development aid by the IsDB (see column 1). Interestingly, we find that hold all other controls constant at their mean, a Shia majority populated country receives on average 86% more of aid than a non-Muslim populated country, while a Sunni majority populated country 52% more. However, it is noteworthy that the statistical significance of Shia populated country is only marginal while the marginal effect of Sunni majority populated country is significantly different from zero at the 5% level.

Surprisingly though, we do not find any statistical significance for any of our control variables with the exception of population which is significantly different from zero at the 1% level across the columns in Table 1. In column 2, we keep basic controls variables only, namely population and GDP per capita. As seen there, controlling only for these variables does not alter our main results which remain intact as reported in column 1. In column 3, we replicate the analysis replacing our main variables of interest - population based on religious sects with religious sects of the regimes in power. As seen, we find significant positive effect of Sunni regimes on aid allocation by IsDB. On the other hand, as expected we do not find any significant impact of Shia regimes. Holding all other control variables constant at their mean, a Sunni regime receives roughly 59% more of IsDB resources than a non-Muslim regime during our study period which is significantly different from zero at the 5% level. A Shia regime, on the other hand, does not receive significantly more IsDB resources than a non-Muslim regime. These results remain robust when we keep basic control variables in column 4 of Table 1. These results clearly lend support for our hypothesis that Sunni regimes are more favored by IsDB over other regimes on aid allocation.

Next, we introduce the interaction terms between our first set of variables capturing population based on religious sects and religious tensions in Table 2. As seen in column 1, we find a negative and statistically significant coefficient of the interaction term. Meaning, Shia majority populated countries receive less development aid from IsDB conditional upon religious tensions in the country between Muslim and non-Muslim religious population. It is noteworthy though that the interaction effect in column 2 of Table 2 becomes statistically insignificant when keeping solely basic control variables. It is important to note that interpretation of the interaction term in non-linear models such as Tobit fixed effects is not similar to interpreting linear models like OLS. A simple t-test on the coefficient of the interaction term is therefore not sufficient to see whether the interaction is statistically

significant (see Ai and Norton 2003, Golder 2003). We rely on the marginal plot as shown in Figure 6, which depicts the magnitude of the interaction effect. To calculate the marginal effect of an additional increase in Shia majority populous country, we take account of both the conditioning variable (religious tensions index) and the interaction term. We show the total marginal effect conditional on religious tensions graphically. The y-axis of Figure 6 displays the marginal effect of Shia majority populous country and on the x-axis the level of religious tensions index at which the marginal effect is evaluated. Moreover, we include the 90% confidence interval in the Figure. As seen there, in line with our results of the Tobit fixed effects estimation, being a Shia majority populated country would receive more development aid from IsDB (at the 90% confidence level at least) if religious tensions index is in the range of 0-4 (which is high to moderate levels of religious tensions in a country). Figure 6 also shows that Shia majority populous country is not favored by IsDB when the religious tensions index is above 4 on a scale of 0-6 where highest value denotes no religious tensions. In other words, the marginal effects are not significant when the higher bound of the confidence interval is below zero. Note that the effects are almost similar (i.e. when religious tensions index is above 4 on a scale of 0-6) when estimating the marginal plot graphically when including only basic control variables as in column 1. These results lend support to our second hypothesis that the power politics of the Sunni-Shia divide does not really influence IsDB's aid allocation decisions especially when Shia majority populated countries confront a higher degree of religious tensions with non-Muslim religious communities.

Next, we replicate the same results by controlling for two-way fixed effects in columns 3-4 in Table 2. Note that that the time invariant component is no longer present in our model when the time invariant variables (regime categories) are interacted with time varying variables (religious tensions index), allowing us to control for country fixed effects. As seen from column 3, the interaction coefficient becomes statistically insignificant once we

control for fixed effects. However, as noted earlier, interpreting the interaction effects in a non-linear model is not straight forward as the statistical significance can vary at various at minimum and maximum values of the interaction term. Like before, we resort to the marginal plot to provide graphical interpretation of the magnitude of the interaction effect. On the y-axis of Figure 7 we show the marginal effect of an increase in Shia majority populated country and on the x-axis the religious tensions index at which the marginal effect is evaluated. As before, we include the 90% confidence interval in the Figure. Figure 7 shows that a Shia populous state is allocated higher amount of development aid by IsDB (at the 90% confidence level at least) if religious tensions index is below 2.5 on a scale of 0-6. This also means that the marginal effects are not significant when the lower bound of the confidence interval is below zero. Interestingly, these effects are much higher (i.e. religious tensions index is below 4.5 on a scale of 0-6) when estimating the marginal plot graphically when excluding the control variables which remains statistically insignificant in column 3.

Turning to the interactions between the religious sects of the regime in power and religious tensions in Table 3, we find that none of the interaction coefficients are statistically significant. The marginal effect of Shia regimes remains statistically insignificant at any level of the religious tensions index. However, it is noteworthy that in column 1 and 3 Sunni regime variable continuous to remain positive and significantly different from zero at conventional levels of statistical significance. These results highlight two important things. First, Sunni regimes are always preferred to Shia and other regimes by IsDB aid allocation irrespective of the level of religious tensions. Second, religious sect of population also matters for IsDB, but this are subject to religious tensions in these countries. Not only Sunni majority populous countries are preferred but also with large Shia populous countries especially when facing higher degree of religious tensions.

With respect to the results on control variables, we find some evidence in favor of need based determinants. We find that populous countries and countries with lower per capita incomes receive development aid from IsDB. Note that both these variables are significantly different from zero at the conventional levels of statistical significance across the models. Holding all other controls at their mean, a one percent increase in per capita income (logged) is associated with a corresponding increase in aid allocation by roughly 0.13 US$ million by IsDB (see column 1, Table 1). However, we do not find any statistical significance on other control variables. Interestingly, we do not find any influence of Saudi Arabia government's bilateral development aid allocation on the aid allocation from IsDB suggesting that having bilateral economic cooperation with Saudi Arabia need not necessarily receive a higher amount of development aid from IsDB.

4.1 Tests for robustness

We examine the robustness of our main findings in several ways. First, we replace our dependent variable with aid commitments from World Bank. If our results are truly driven by the power politics of Sunni-Shia divide, then World Bank's aid commitments must not be influenced by our main variables of interests. We report these results in Table 4. As seen there, we do not find any correlation between the variables capturing Sunni-Shia divide on aid allocation decisions of the World Bank. Neither the population based on religious sects not the religious sects of the regime in power could explain the World Bank commitments to these countries under study during our study period. On the contrary, we find several control variables which remains insignificant in our previous models, now gain statistical significance. For instance, we find that World Bank commitments are influenced by need based factors in the recipient countries. Likewise, countries which face economic crisis, measured as debt crisis, do receive higher amount of aid from World Bank. Similarly, countries with a lower share of international foreign exchange reserves receive aid

commitments from the World Bank. These results lend support to our hypotheses and validate our main set of results that religious politics is the main driver behind aid allocation decisions of IsDB.

Second, we also estimate our models reported in Table 1-3 with OLS estimation specifications. Replicating our results using OLS specifications does not alter our main findings reported in Table 1-3. Third, we also add additional control variables to get a more detailed picture of whether and to what extent our main findings are driven by the specific choice of explanatory variables out of the larger set of theoretically plausible determinants. We thus collected some additional variables which could influence IsDB aid allocation namely, Foreign Direct Investments (FDI) as a share of GDP, Domestic investments proxied by Gross Fixed Capital Formation (GFCF) as a share of GDP, Per capita GDP (squared), a dummy variable indicating whether a country is a member of Organization of the Petroleum Exporting Countries (OPEC). Most of the development aid from IsDB is technical in nature intended to promote investments and industrialization process in these countries. Thus, we expect that countries with lower levels of foreign and domestic investments must be associated with higher levels of development aid from IsDB. Likewise, we also expect that countries which are major global oil producers could receive lower amount of aid vis-à-vis countries which are not dependent on natural resources. The inclusion of these additional variables does not alter the above comparisons. Note that due to brevity, we do not report the robustness check findings here, but they are available upon request.

Conclusions

This paper analyzes loan allocation patterns by the IsDB during the period 1976-2007 to investigate to what the extent the prominent Sunni-Shia divide of Islamic societies is refracted to the politics of the region's largest development aid donor. This order is

attributable to governance imbalances across member states of Bank, a common feature in IFIs primarily linked to differences in capital contributions as well as to institutional missions. Here in particular, Saudi Arabia is by far the largest shareholder of the IsDB and a noteworthy pro-Sunni regime, and therefore we expected Bank lending to follow this country's political stance in the Islamic world. Our empirical results support this view. Member countries in which the head of state is Sunni-Islam affiliated receive on average 59% more in resources from the IsDB every year than that Shia-Islam affiliated. Islamic solidarity across both sects prevails, however, during conflictive periods with other non-Islamic religious groups and discrimination towards Shias vanishes temporarily. Member states with large Shia populations do in fact receive significantly more loans from the IsDB in scenarios of high religious tensions. An equivalent examination of the allocation patterns by the World Bank to the same group of countries and during the same time frame confirms that the dynamics of religiously motivated lending are only inherent to the IsDB.

Criticism to IFIs is usually associated to major Western countries exerting control over the availability of aid resources to developing countries in order to favor their own interests. This study shows that IFIs in which major Western countries do not intervene nor participate of their lending decisions are neither exempt of political manipulation. Ironically, the surge of Arab donors responds largely to the relative neglect of DAC donors and their sponsored IFIs in serving Islamic countries. The structure and governance of the IsDB is virtually dominated by Saudi Arabia together with other pro-Sunni regimes and selectivity to access to funds based on religious principles is rather difficult to avoid. The IsDB will only gain credibility and transparency as a regional development institution after it assimilates the whole spectrum of Islamic societies in its organization.

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Table 1: IsDB Commitments and Religious affiliation of Population, Tobit (1976-2007)

	(1)	(2)	(3)	(4)
Population (log)	**0.244*** **	**0.163*** **	**0.223** **	**0.165*** **
	(0.00566)	**(0.00112)**	**(0.0103)**	**(0.000894)**
GDP per capita (log)	-0.0959	**-0.172** **	-0.118	**-0.163** **
	(0.403)	**(0.0310)**	(0.300)	**(0.0310)**
Democracy (dummy)	-0.256		-0.268	
	(0.355)		(0.337)	
Civil war (dummy)	0.0227		0.0585	
	(0.903)		(0.745)	
Saudi Arabia aid (log)	-0.00643		-0.00973	
	(0.730)		(0.606)	
Trade/GDP	0.00284		0.00376	
	(0.399)		(0.268)	
Oil production (log)	-0.0162		-0.0109	
	(0.194)		(0.401)	
International Reserves/GDP	-0.00914		-0.0112	
	(0.226)		(0.124)	
Debt crisis (dummy)	0.246		0.203	
	(0.793)		(0.827)	
Sunni populous country (dummy)	**0.523** **	**0.538** **		
	(0.0255)	**(0.0174)**		
Shia populous country (dummy)	**0.816***	**0.714***		
	(0.0558)	**(0.0572)**		
Sunni Regime (dummy)			**0.584** **	**0.541** **
			(0.0170)	**(0.0269)**
Shia Regime (dummy)			0.536	0.472
			(0.127)	(0.150)
Constant	**11.94*** **	**13.46*** **	**12.32*** **	**13.38*** **
	(6.86e-11)	**(0)**	**(0)**	**(0)**
Country fixed effects	No	No	No	No
Time fixed effects	Yes	Yes	Yes	Yes
Number of Countries				
Total Observations	306	327	306	327

Notes: The dependent variable is the loan commitments approved by the Islamic Development Bank (IsDB) to borrowing member *i* in period *t*, denominated in US constant dollars (base year 2000) and in logarithmic scale. Standard errors are robust; p-values are reported in brackets. *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$.

Table 2: IsDB Commitments, Religious Affiliation of Population and Religious Tensions, Tobit (1976-2007)

	(1)	(2)	(3)	(4)
Population (log)	**0.221***	0.0899	2.068	2.354
	(0.0856)	(0.266)	(0.225)	(0.143)
GDP per capita (log)	-0.132	**-0.269*****	-0.308	**-0.561***
	(0.364)	**(0.00219)**	(0.381)	**(0.0805)**
Democracy (dummy)	-0.326		0.363	
	(0.315)		(0.192)	
Civil war (dummy)	-0.0273		-0.128	
	(0.921)		(0.654)	
Saudi Arabia aid (log)	-0.00871		0.0240	
	(0.715)		(0.282)	
Trade/GDP	0.000694		0.0128	
	(0.866)		(0.185)	
Oil production (log)	-0.0269		0.00891	
	(0.142)		(0.701)	
International Reserves/GDP	-0.00659		0.00412	
	(0.422)		(0.659)	
Debt crisis (dummy)	1.259		-0.684	
	(0.407)		(0.687)	
Sunni populous country (dummy)	**0.905*****	**0.882*****	**0.279**	**1.409***
	(0.00232)	**(0.00159)**	**(0.779)**	**(0.0867)**
Shia populous country (dummy)	**4.761*****	**2.579****	**9.422****	**11.85*****
	(0.00474)	**(0.0112)**	**(0.0268)**	**(0.00288)**
Religious Tensions	0.0346	0.0349	0.0442	0.0658
	(0.682)	(0.644)	(0.727)	(0.589)
Shia populous country × Religious Tensions	**-0.919****	-0.444	**-1.222*****	**-1.200*****
	(0.0246)	(0.116)	**(6.16e^{-06})**	**(1.57e^{-05})**
Constant	**12.36*****	**14.86*****	-19.20	-22.21
	(4.24e^{-06})	**(0)**	(0.519)	(0.426)
Country fixed effects	No	No	Yes	Yes
Time fixed effects	Yes	Yes	Yes	Yes
Number of Countries				
Total Observations	207	215	207	215

Notes: The dependent variable is the loan commitments approved by the Islamic Development Bank (IsDB) to borrowing member *i* in period *t*, denominated in US constant dollars (base year 2000) and in logarithmic scale. Specifications 3 and 4 control for country fixed effects. Standard errors are robust; p-values are reported in brackets. *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$.

Table 3: IsDB Commitments, Religious Affiliation of Head of State and Religious Tensions, Tobit (1976-2007)

	(1)	(2)	(3)	(4)
Population (log)	0.168	0.111	2.084	2.633
	(0.176)	(0.155)	(0.221)	(0.109)
GDP per capita (log)	-0.214	**-0.264*** **	-0.127	-0.251
	(0.184)	**(0.00182)**	(0.749)	(0.529)
Democracy (dummy)	-0.375		0.428	
	(0.261)		(0.130)	
Civil war (dummy)	0.149		-0.0447	
	(0.562)		(0.882)	
Saudi Arabia aid (log)	-0.0116		0.0339	
	(0.632)		(0.164)	
Trade/GDP	0.00419		0.0129	
	(0.317)		(0.209)	
Oil production (log)	-0.0161		0.0163	
	(0.427)		(0.495)	
International Reserves/GDP	-0.0114		0.00266	
	(0.174)		(0.829)	
Debt crisis (dummy)	0.876		-0.859	
	(0.580)		(0.610)	
Sunni Regime (dummy)	**1.041*** **	**0.929*** **	-0.783	-1.391
	(0.00130)	**(0.00371)**	(0.791)	(0.434)
Shia Regime (dummy)	0.592	1.323	1.141	0.967
	(0.706)	(0.172)	(0.720)	(0.653)
Religious Tensions	0.0334	0.0423	-0.00353	-0.00341
	(0.714)	(0.601)	(0.978)	(0.978)
Shia Regime × Religious Tensions	0.0505	-0.147	0.386	0.265
	(0.886)	(0.514)	(0.389)	(0.560)
Constant	**13.48*** **	**14.43*** **	-23.04	-29.27
	(4.08e^{-07})	**(0)**	(0.432)	(0.297)
Country fixed effects	No	No	Yes	Yes
Time fixed effects	Yes	Yes	Yes	Yes
Number of Countries				
Total Observations	207	215	207	215

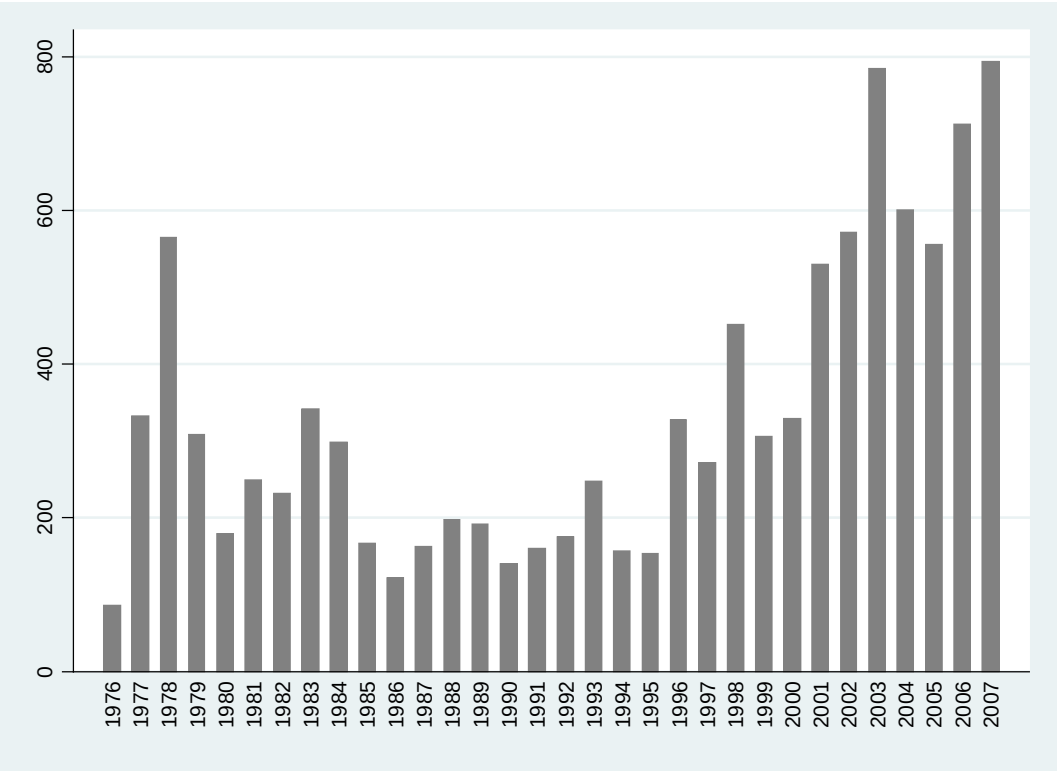
Notes: The dependent variable is the loan commitments approved by the Islamic Development Bank (IsDB) to borrowing member *i* in period *t*, denominated in US constant dollars (base year 2000) and in logarithmic scale. Specifications 3 and 4 control for country fixed effects. Standard errors are robust; p-values are reported in brackets. *** p < 0.01, ** p < 0.05, * p < 0.1.

Table 4: World Bank Commitments, Religious Affiliation of Population and Head of State, Tobit, (1976-2007)

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Population (log)	**2.652*** **	**2.585*** **	**2.683*** **	**2.587*** **	**2.639*** **	**2.643*** **	**2.670*** **	**2.627*** **
	(0)	**(0)**	**(0)**	**(0)**	**(0)**	**(0)**	**(0)**	**(0)**
GDP per capita (log)	**-2.852*** **	**-2.813*** **	**-2.799*** **	**-2.808*** **	**-2.890*** **	**-2.854*** **	**-2.845*** **	**-2.896*** **
	(7.35e-09)	**(5.61e-09)**	**(1.75e-08)**	**(1.21e-08)**	**(2.05e-08)**	**(1.01e-08)**	**(1.38e-08)**	**(2.22e-08)**
Democracy (dummy)	1.333	1.174	1.342	1.173	1.305	1.265	1.360	1.264
	(0.159)	(0.216)	(0.161)	(0.216)	(0.170)	(0.189)	(0.152)	(0.187)
Civil war (dummy)	**-5.022*** **	**-4.638*** **	**-4.988*** **	**-4.631*** **	**-5.077*** **	**-5.017*** **	**-5.059*** **	**-5.062*** **
	(2.61e-05)	**(0.000121)**	**(2.81e-05)**	**(0.000118)**	**(1.88e-05)**	**(2.85e-05)**	**(2.25e-05)**	**(2.25e-05)**
Saudi Arabia aid (log)	**0.279** **	**0.276** **	**0.297*** **	**0.277** **	**0.280** **	**0.291*** **	**0.285** **	**0.282** **
	(0.0139)	**(0.0115)**	**(0.00929)**	**(0.0143)**	**(0.0130)**	**(0.00830)**	**(0.0132)**	**(0.0138)**
Trade/GDP	-0.0199	-0.0172	-0.0202	-0.0172	-0.0207	-0.0210	-0.0202	-0.0210
	(0.246)	(0.325)	(0.240)	(0.325)	(0.228)	(0.223)	(0.237)	(0.222)
Oil production (log)	-0.101	-0.0843	**-0.106***	-0.0845	-0.0956	-0.0952	**-0.104***	-0.0915
	(0.102)	(0.164)	**(0.0813)**	(0.166)	(0.136)	(0.142)	**(0.0900)**	(0.167)
International Reserves/GDP	**-0.0811** **	**-0.0789** **	**-0.0839** **	**-0.0791** **	**-0.0837** **	**-0.0825** **	**-0.0838** **	**-0.0832** **
	(0.0194)	**(0.0174)**	**(0.0148)**	**(0.0176)**	**(0.0156)**	**(0.0173)**	**(0.0149)**	**(0.0165)**
Debt crisis (dummy)	**9.107** **	**8.039***	**8.430***	**7.976***	**9.031** **	**8.519***	**8.978** **	**8.850** **
	(0.0414)	**(0.0647)**	**(0.0595)**	**(0.0701)**	**(0.0435)**	**(0.0517)**	**(0.0447)**	**(0.0461)**
Sunni populous country (dummy)	0.555			-0.0711				
	(0.490)			(0.929)				
Shia populous country (dummy)		-3.040		-3.095				
		(0.139)		(0.147)				
Other populous country (dummy)			0.290					
			(0.717)					
Sunni Regime (dummy)					0.534			0.419
					(0.507)			(0.606)
Shia Regime (dummy)						-0.741		-0.437
						(0.673)		(0.813)
Other Regime (dummy)							-0.317	
							(0.697)	
Constant	-6.132	-5.231	-6.607	-5.237	-5.590	-5.509	-5.917	-5.269
	(0.422)	(0.492)	(0.392)	(0.492)	(0.474)	(0.487)	(0.445)	(0.509)
Country fixed effects	No	No	No	No	No	No	No	No
Time fixed effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	359	359	359	359	359	359	359	359

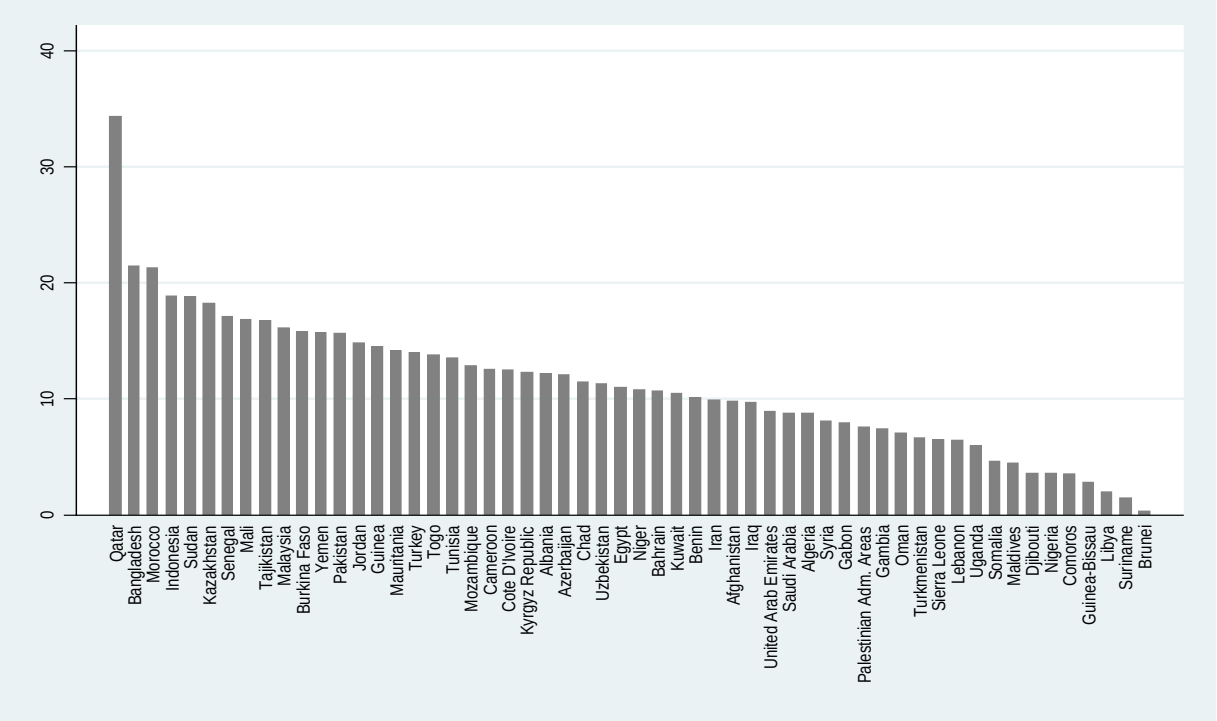
Notes: The dependent variable is the loan commitments approved by the World Bank to borrowing member i in period t, denominated in US constant dollars (base year 2000) and in logarithmic scale. Standard errors are robust; p-values are reported in brackets. *** p < 0.01, ** p < 0.05, * p < 0.1.

Figure 1: IsDB Commitments, Millions of 2000 US Constant Dollars.



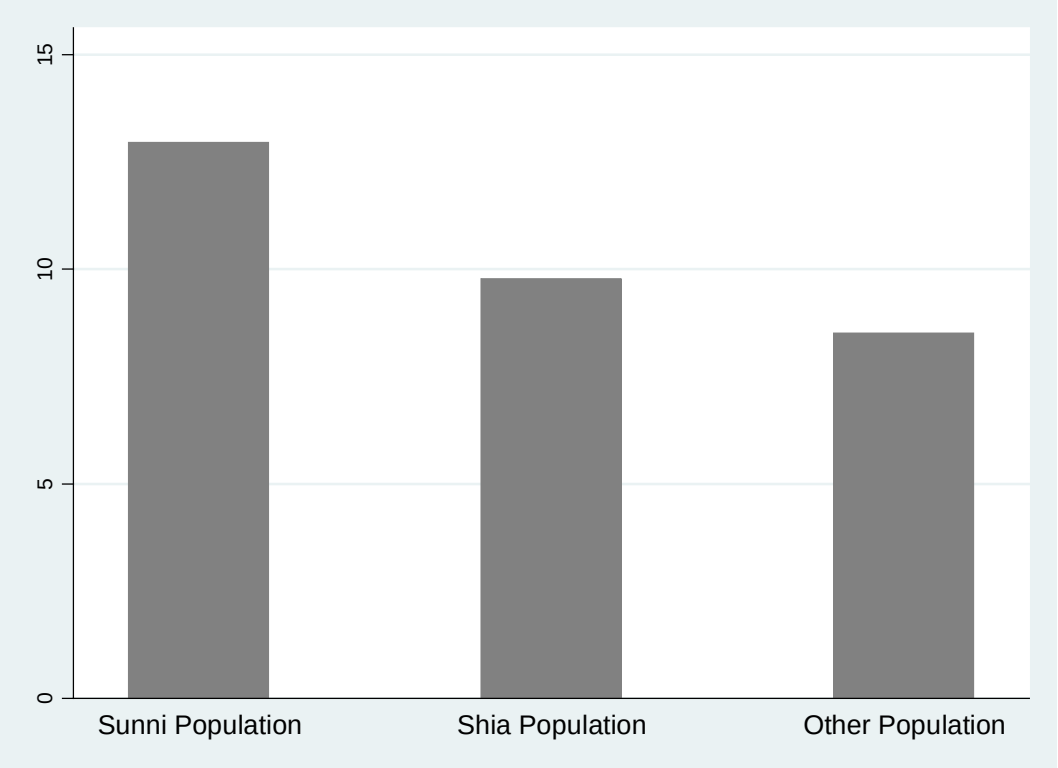
Notes: The graph shows loan commitments approved by the Islamic Development Bank (IsDB) in each year for the period 1976-2007. Figures are given in US constant dollars (base year 2000) and scaled to millions. Source: IsDB, OECD.

Figure 2: IsDB Commitments by Borrowing Member, Yearly Average in 1976-2007 (Millions of 2000 US Constant Dollars)



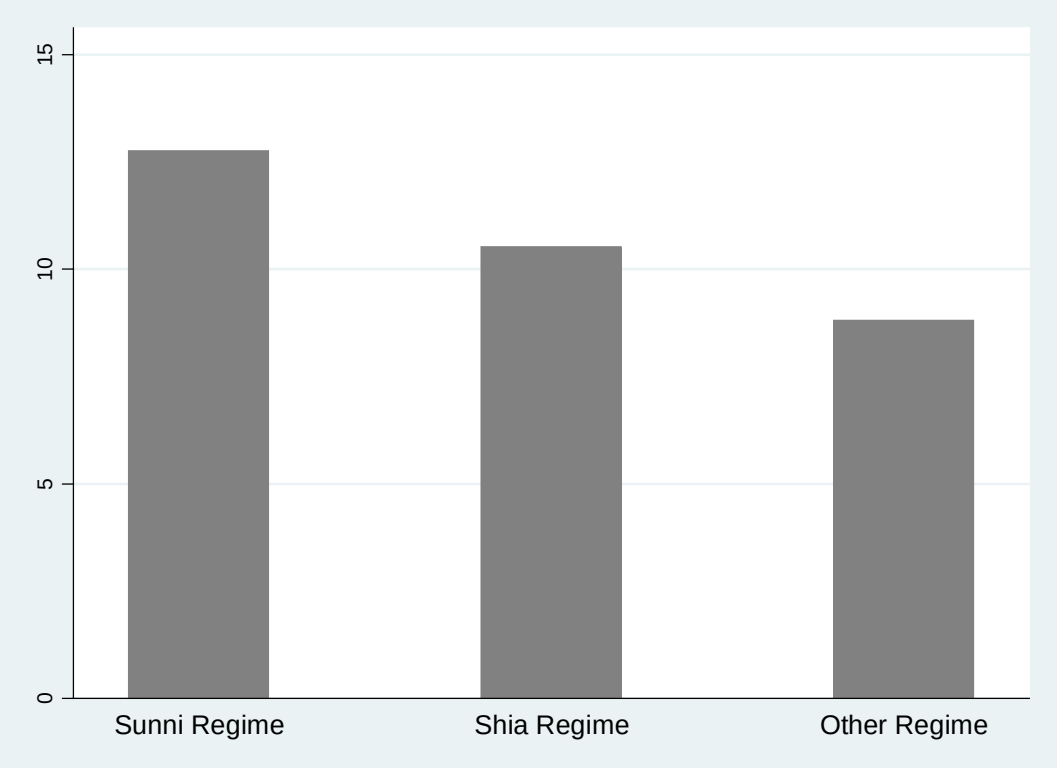
Notes: The graph shows loan commitments approved by the Islamic Development Bank (IsDB) to each borrowing member on average every year over the period 1976-2007. Figures are given in US constant dollars (base year 2000) and scaled to millions. Source: IsDB, OECD.

Figure 3: IsDB Commitments by Religious Affiliation of Population, Yearly Average in 1976-2007 (Millions of 2000 US Constant Dollars)



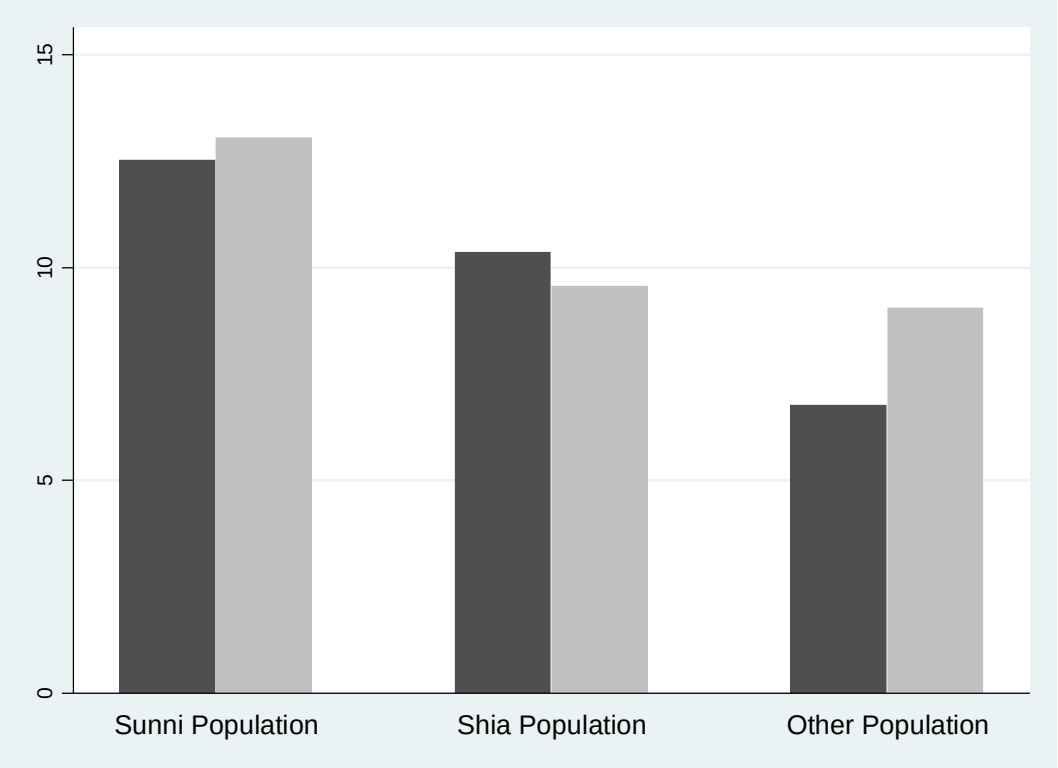
Notes: "Sunni Population" identifies borrowing members where at least 50% of the population is affiliated to Sunni Islam, "Shia Population" identifies borrowing members where at least 50% of the population is affiliated to Shia Islam or any other Islam sect different to Sunni Islam, and "Other Population" identifies borrowing members where at least 50% of the population is affiliated to a religion different to Islam. Figures are given in US constant dollars (base year 2000) and scaled to millions. **Source:** IsDB, OECD, Pew Research Center.

Figure 4: IsDB Commitments by Religious Affiliation of Head of State, Yearly Average in 1976-2007 (Millions of 2000 US Constant Dollars)



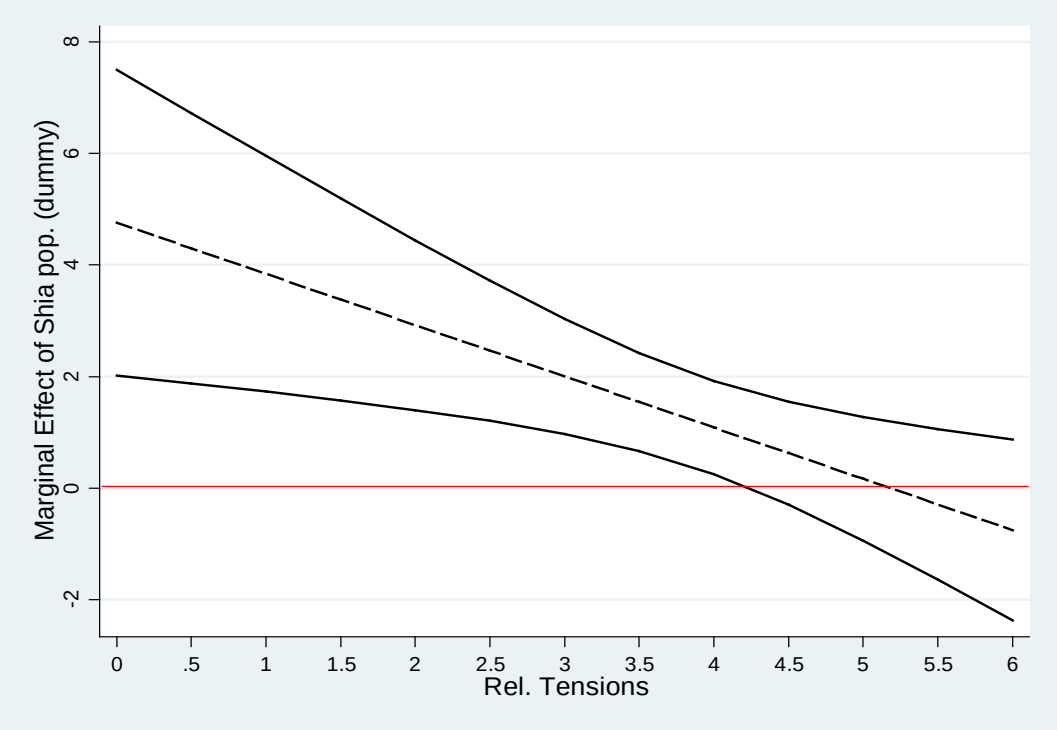
Notes: "Sunni Regime" identifies borrowing members whose head of state is affiliated to Sunni Islam, "Shia Population" identifies borrowing members whose head of state is affiliated to Shia Islam or any other Islam sect different to Sunni Islam, and "Other Population" identifies borrowing members whose head of state is affiliated to a religion different to Islam. Figures are given in US constant dollars (base year 2000) and scaled to millions. **Source:** IsDB, OECD, CIA World Fact Book, Encyclopedia Britannica.

Figure 5: IsDB Commitments by Religious Affiliation of Population and Religious Tensions, Yearly Average in 1976-2007 (Millions of 2000 US Constant Dollars)



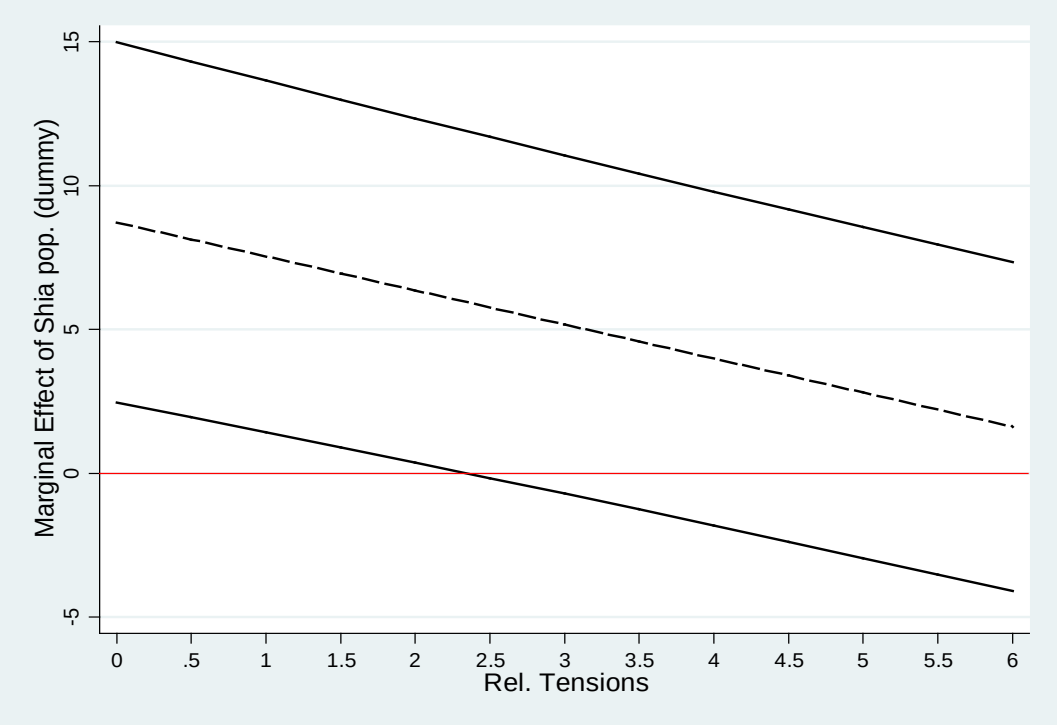
Notes: The graph shows loan commitments approved by the Islamic Development Bank (IsDB) to each borrowing member whose population is of a certain religious affiliation and confronting a determined level of religious tensions, on average every year over the period 1976-2007. "Sunni Population" identifies borrowing members where at least 50% of the population is affiliated to Sunni Islam, "Shia Population" identifies borrowing members where at least 50% of the population is affiliated to Shia Islam or any other Islam sect different to Sunni Islam, and "Other Population" identifies borrowing members where at least 50% of the population is affiliated to a religion different to Islam. Dark bars denote for borrowing members experiencing high religious tensions in a given a year (Religious Tensions Index between 0 and 3), light bars denote for borrowing members experiencing low religious tensions in a given year (Religious Tension Index between 3 and 6). Figures are given in US constant dollars (base year 2000) and scaled to millions. **Source:** IsDB, OECD, Pew Research Center, ICRG.

Figure 6: Conditional Marginal Effects of Shia Population on IsDB Commitments, Country Fixed Effects Excluded, 90% Confidence Interval.



Notes: The graph shows the marginal effects of Shia population (dummy) on IsDB loan commitments (log). Marginal effects are conditioned to different values of the religious tensions index. Dashed lines denote upper and lower boundaries of the 90% confidence interval.

Figure 7: Conditional Marginal Effects of Shia Population on IsDB Commitments, Country Fixed Effects Included, 90% Confidence Interval



Notes: The graph shows the marginal effects of Shia population (dummy) on IsDB loan commitments (log). Marginal effects are conditioned to different values of the religious tensions index. Dashed lines denote upper and lower boundaries of the 90% confidence interval.

Appendix

Appendix 1: List of Countries under study

Afghanistan	**Egypt**	**Malaysia**	**Sierra Leone**
Albania	Gabon	**Maldives**	**Somalia**
Algeria	**Gambia**	**Mali**	**Sudan**
Azerbaijan	**Guinea**	**Mauritania**	Surinam
Bahrain	Guinea-Bissau	**Morocco**	**Syria**
Bangladesh	**Indonesia**	Mozambique	**Tajikistan**
Benin	**Iran**	**Niger**	Togo
Brunei	**Iraq**	Nigeria	**Tunisia**
Burkina Faso	**Jordan**	**Oman**	**Turkey**
Cameroon	**Kazakhstan**	**Pakistan**	**Turkmenistan**
Chad	**Kuwait**	**Palestinian Adm. Areas**	Uganda
Comoros	**Kyrgyz Republic**	**Qatar**	**United Arab Emirates**
Cote d'Ivoire	Lebanon	**Saudi Arabia**	**Uzbekistan**
Djibouti	**Lybia**	**Senegal**	**Yemen**

Notes: Palestinian Administrated Areas is officially represented and an active member in the IsDB. However it falls out the empirical analysis given data unavailability for control variables. Highlighted countries are Muslim majority populated.

Appendix 2: Data definition and sources

Variables	Description	Source
IsDB commitments	IsDB loan commitments received by a borrowing member in a year in constant dollars.	IsDB Annual Report (various years), OECD (2012).
WB commitments	World Bank loan commitments received by a borrowing member in a year in constant dollars.	OECD (2012).
Population	Total population.	World Bank (2012).
GDP per capita	GDP per capita in current dollars.	World Bank (2012).
Democracy	Dummy coded 1 if government is democratic, and 0 otherwise.	Cheibub et al. (2010).
Civil war	Dummy coded 1 if recipient undergoes a civil war, and 0 otherwise.	Gleditsch et al. (2002).
Saudi Arabia aid	Saudi Arabia bilateral aid received by a borrowing member in a year in constant dollars.	OECD (2012).
Trade to GDP	Sum of merchandise exports and imports in percentage of GDP.	World Bank (2012).
Oil production	Value of oil production in constant dollars.	Ross (2011).
International Reserves to GDP	International reserves in percentage of total GDP.	World Bank (2012).
Debt crisis	Dummy coded 1 if recipient undergoes a debt crisis, and 0 otherwise.	Laeven and Valencia (2012).
Sunni population	Dummy coded 1 if religious affiliation of at least 50% of the population is Sunni Islam, and 0 otherwise.	Pew Research Center (2013).
Shia population	Dummy coded 1 if religious affiliation of at least 50% of the population is Shia Islam, and 0 otherwise.	Pew Research Center (2013).
Other population	Dummy coded 1 if religious affiliation of at least 50% of the population is not Islam (any sect), and 0 otherwise.	Pew Research Center (2013).
Sunni regime	Dummy coded 1 if religious affiliation of borrowing member government in a year is Sunni Islam, and 0 otherwise.	CIA World Fact Book (2013), Encyclopedia Britannica (2012).
Shia regime	Dummy coded 1 if religious affiliation of borrowing member government in a year is Shia Islam, and 0 otherwise.	CIA World Fact Book (2013), Encyclopedia Britannica (2012).
Other regime	Dummy coded 1 if religious affiliation of borrowing member government in a year is not Islam (any sect), and 0 otherwise.	CIA World Fact Book (2013), Encyclopedia Britannica (2012).
Religious Tensions	Religious Tension Index, from 0 (highest) to 6 (lowest).	International Country Risk Guide (2012).

Appendix 3: Descriptive Statistics

Variables	Obs.	Mean	Std. Dv.	Minimum	Maximum
IsDB commitments (log)	346	15.25	1.48	6.11	17.58
WB commitments (log)	448	10.56	8.25	0.00	21.68
Population (log)	427	15.65	1.64	11.89	19.24
GDP per capita (log)	398	6.95	1.40	4.68	10.93
Democracy (dummy)	420	0.13	0.32	0.00	1.00
Civil war (dummy)	420	0.24	0.38	0.00	1.00
Saudi Arabia aid (log)	448	2.82	4.39	0.00	19.25
Trade/GDP	383	58.37	31.38	10.40	213.19
Oil production (log)	429	12.98	10.35	0.00	25.86
International Reserves/GDP	363	13.84	14.96	0.09	141.46
Debt crisis (dummy)	417	0.01	0.06	0.00	0.25
Sunni populous (dummy)	430	0.71	0.45	0.00	1.00
Shia populous (dummy)	430	0.09	0.28	0.00	1.00
Other populous (dummy)	430	0.20	0.40	0.00	1.00
Sunni regime (dummy)	430	0.72	0.45	0.00	1.00
Shia regime (dummy)	430	0.09	0.28	0.00	1.00
Other regime (dummy)	430	0.19	0.39	0.00	1.00
Religious Tensions	257	3.52	1.41	0.00	6.00