IFC’s hidden lending motives

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1) Background

The International Finance Corporation

“Our goals are to end extreme poverty by 2030 and boost shared prosperity in every developing country” (ifc.org)

- World Bank Group member (but no ODA)
- Loans with longer maturity, technical advice, reputation
- Rising influence (2011: 18.6 bn US$ → 7% of DAC’s ODA)
- Largest global development institution focused exclusively on the private sector in developing countries (DCs)
1) Background

The International Finance Corporation

“Our goals are to **end extreme poverty** by 2030 and **boost shared prosperity** in every developing country” (ifc.org)

- 65% of loans to large conglomerates (operators) in rich countries which invest in DCs vs. 16% to companies in DCs
  - Loans increase companies’ competitive advantage
  - IFC has unfair competitive advantage (no taxes on earnings and income, best refinancing opportunities)
- Disputable benefit to the local economy of a DC

➢ **Best strategy to boost development and eradicate poverty?**
2) Hypothesis

IFC’s hidden lending motives

The joint influence of recipients and project operators, when their home countries are both represented as IFC board members, UNSC members or UNGA members voting in line with the US leads to increased IFC lending.

- **UNGA:** US loans/grants increased for recipients voting in line (e.g., Dreher, Nunnenkamp & Thiele 2008)
- **IMF:** loans for membership in the **UNSC** (Dreher, Sturm & Vreeland 2009)
- **IBRD:** larger funding for **board member countries** (Kaja & Werker 2010)

➢ New approach: project operators, joint influence and IFC lending
3) Empirical strategy

Dyadic regression

\[
y_{ijt} = \beta_1 \text{Position}_{it} + \beta_2 \text{Position}_{jt} + \beta_3 \text{Position}_{it} \times \text{Position}_{jt} + \Sigma \beta_4 \text{Controls}_{it} + \Sigma \beta_5 \text{Controls}_{jt} + \eta_i + \delta_j + \mu_t + e_{ijt}
\]

\(y_{ijt}\): IFC-lending (US$) / project number between a recipient i and project operator j in year t.

\(\text{Position}\): IFC director, UNSC member, US voting alignment UNGA

<table>
<thead>
<tr>
<th>Recipient country level</th>
<th>Operator country level</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Kaja &amp; Werker 2010 specification (for WB directors)</td>
<td>• Event time specification (-2, -1, +1)</td>
</tr>
<tr>
<td>• Event time specification (-2, -1, +1)</td>
<td>• Event time specification (-2, -1, +1)</td>
</tr>
<tr>
<td>• Alternate in board +</td>
<td>• Alternate in board +</td>
</tr>
<tr>
<td>• Board voting power +</td>
<td>• Board voting power +</td>
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<tr>
<td>• Bank voting power +</td>
<td>• Bank voting power +</td>
</tr>
<tr>
<td>• Population size +</td>
<td>• Population size +</td>
</tr>
<tr>
<td>• Democracy +</td>
<td>• Democracy +</td>
</tr>
<tr>
<td>• Major war occurrence –</td>
<td>• Access to finance –</td>
</tr>
<tr>
<td>• Access to finance –</td>
<td>• Bilateral trade flows +</td>
</tr>
<tr>
<td>• Investment profile – / +</td>
<td></td>
</tr>
</tbody>
</table>
4) Preliminary results
IFIC board member

Data: 2000-2011, 184 IFC member countries, 1943 projects

<table>
<thead>
<tr>
<th>VARIABLES</th>
<th>(1) Project number</th>
<th>(2) Project number</th>
<th>(3) IFC investment</th>
<th>(4) IFC investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operator director * Recipient director</td>
<td>0.0480**</td>
<td>0.0593***</td>
<td>0.8027**</td>
<td>0.9901***</td>
</tr>
<tr>
<td></td>
<td>[0.011]</td>
<td>[0.010]</td>
<td>[0.011]</td>
<td>[0.010]</td>
</tr>
<tr>
<td>Operator director</td>
<td>-0.0064**</td>
<td>-0.0105**</td>
<td>-0.1061**</td>
<td>-0.1761**</td>
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<tr>
<td></td>
<td>[0.024]</td>
<td>[0.021]</td>
<td>[0.024]</td>
<td>[0.021]</td>
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<tr>
<td>Recipient director</td>
<td>-0.0070***</td>
<td>-0.0092***</td>
<td>-0.1157***</td>
<td>-0.1536***</td>
</tr>
<tr>
<td></td>
<td>[0.006]</td>
<td>[0.009]</td>
<td>[0.006]</td>
<td>[0.009]</td>
</tr>
<tr>
<td>Controls</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Observations</td>
<td>406,272</td>
<td>219,988</td>
<td>406,272</td>
<td>219,988</td>
</tr>
<tr>
<td>R-squared</td>
<td>0.012</td>
<td>0.015</td>
<td>0.012</td>
<td>0.015</td>
</tr>
<tr>
<td>No. recipients</td>
<td>184</td>
<td>128</td>
<td>184</td>
<td>128</td>
</tr>
<tr>
<td>No. project operators</td>
<td>184</td>
<td>128</td>
<td>184</td>
<td>128</td>
</tr>
</tbody>
</table>

Robust pval in brackets *** p<0.01, ** p<0.05, * p<0.1, Standard errors clustered by dyad

• Robust results for different specifications (including event-time specification)
• Same findings for UNSC membership and US voting alignment in UNGA
5) Preliminary conclusions

Coalitions matter

1. Operator-recipient coalitions in board get more projects with higher funding approved

2. Same relationship for other important positions (UNSC membership or voting alignment in the UNGA)

3. No positive effect for operators or recipients in board alone

- Twofold distortion of competition
  - Among companies: beneficial to large companies
  - Among financial institutions: detrimental to private financial institutions
6) Next steps

Further questions

• Influential recipient-operator coalitions get more - who gets less?
• Do coalition projects involve higher social or environmental risks?
• Do coalition-countries also get more IFC-funding overall?
• Potential trade-off between IBRD- and IFC-lending?

Extensions and robustness

• Code all projects (1995-2016)
• Test the influence of board membership tenure (currently coded)
• Check different dates in project circle (disclosed, board projected, signed)
• Implement half-year lag (board members change in July)
• Include time-invariant country-pair controls (language, distance, etc.)
• Test non-linear regression models
Thanks for your attention.
Backup

IFC board membership

Board of executive directors

- 25 directors approve each project
- Five permanent seats (directors appointed by largest shareholders)
- 20 seats elected by votes of all member countries
- Two-year terms
- Each director appoints one alternate
Backup
IFC board, UNSC, US voting alignment UNGA

Channels of influence

1. WB internal network: Among directors and departments (prepare project proposals)

2. WB external network: Director part of network meetings (e.g., embassy)

3. Recipients and project operators execute political influence via important positions (UNSC and UNGA voting)
   - Lobby for themselves and each other