THE EFFECTIVENESS OF IDB’S FOREIGN AID ON ECONOMIC GROWTH: AN EMPIRICAL STUDY OF AFRICAN MUSLIM COUNTRIES

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THE EFFECTIVENESS OF IDB'S FOREIGN AID ON ECONOMIC GROWTH: AN EMPIRICAL STUDY OF AFRICAN MUSLIM COUNTRIES

By
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Thesis Submitted to the Othman Yeop Abdullah Graduate School of Business, Universiti Utara Malaysia, in Fulfillment of the Requirement for the Degree of Doctor of Philosophy
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The Islamic Development Bank (IDB) is the most leading and prominent Islamic multilateral financial and development institution in the Muslim world. Yet, with its foreign aid activities in almost four decades in various parts of the world, especially in the African continent; it is surprising to note that no empirical study is available on the impact of its foreign aid activities in Africa, particularly the African Muslim Countries (AMCs). The AMCs constitute more than two-third of the member countries of IDB from Africa. Therefore, this study provides empirical evidences from AMCs like Algeria, Egypt, Gambia, Morocco, Nigeria, Senegal, Tunisia and a host of others, on the role of IDB in accounting for growth in these countries spanning 1987-2010 through balanced panel data. Also, this study examined the nature of causality existing between foreign aid and corruption in AMCs. This is in view of the endemic prevalence of corruption in Africa. Hence, Simultaneous Equations Model (SEM) was adopted as the base model; while OLS, 3SLS and Seemingly Unrelated Regressions Estimate (SURE) methods were utilized for its estimation. On the other hand, Autoregressive Distributed Lag (ARDL) approach based on Cointegration and Granger-causality tests were used to estimate for corruption-aid nexus. Evidently, the findings from this study revealed that the foreign aid activities of IDB positively impact on the economic growth of AMCs via investment as the major transmission channel and it thus confirm the aid effectiveness hypothesis. Also, the nature of causality between corruption and foreign aid is both in the short and long-run; and our findings establish that countries like Morocco and Nigeria are victims of corruption trap. Basically, this study is perhaps the first of its kind to empirically investigate the impact of the foreign aid activities of IDB in Africa.

**Key words:** Islamic Development Bank, Foreign Aid, Simultaneous Equations Model, Economic Growth, African Muslim Countries
ABSTRAK


Kata kunci: Bank Pembangunan Islam, Bantuan Asing, Model Persamaan Serentak, Pertumbuhan Ekonomi, African Muslim Countries
ACKNOWLEDGEMENTS

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DECLARATIONS

In accordance with conventional academic research ethics, I hereby declare that some parts of this thesis have been published in the following articles:


TABLE OF CONTENTS

Contents                                                                                     Page
TITLE PAGE                                                                             i
CERTIFICATION OF THESIS                                         ii
PERMISSION TO USE                                                iv
ABSTRACT                                                   v
ABSTRAK                                                    vi
ACKNOWLEDGEMENTS                                               vii
DECLARATIONS                                                  viii
TABLE OF CONTENTS                                              ix
LIST OF APPENDICES                                            xv
LIST OF TABLES                                                xvii
LIST OF FIGURES                                               xix
LIST OF ABBREVIATIONS                                         xx

CHAPTER ONE: INTRODUCTION

1.0 Introduction                              1
1.1 Background of the Study                  1
1.2 Problem Statement                        16
1.3 Research Questions                        22
1.4 Research Objectives                      23
1.5 Significance of the Study                23
1.6 Conceptual Framework                     26
1.6.1 Foreign Aid                            26
1.6.2 Human Capital Development (HCD)       30
1.6.3 African Muslim Countries (AMCs)       37
1.7 Organization of the Thesis               40
3.3.1 IDB Activities in Member Countries: An Overview 109
3.3.2 IDB and Foreign Aid in Africa 118
3.4 Foreign Aid Discourse and Some Pertinent Issues 122
3.4.1 Schools of Thoughts on Aid-Growth Nexus Debate 122
3.4.2 Foreign Aid: Purpose and Motives 124
3.4.3 Bilateral Aid versus Multilateral Aid 128
3.4.4 Fundamental Principles of Multilateral Aid 131
3.4.5 Foreign Aid as an Economic and Political Tool 134
3.4.6 Foreign Aid and Donors’ Conditionality 136
3.4.7 Moral Hazard and the Concept of Aid Fungibility 138
3.5 Islamic Perspective of Foreign Aid 139

CHAPTER FOUR: METHODOLOGY

4.0 Introduction 147
4.1 Methodological Framework 147
4.1.1 Analytical Framework 151
4.1.1.1 Hypotheses/Propositions Development 153
4.2 Model Specification 154
4.2.1 Simultaneous Equations Model (SEM) 154
4.2.2 The Twin Issues of Identification in SEM 157
4.2.2.1 Application of the Order Condition 158
4.2.2.2 Application of the Rank Condition 159
4.3 Research Methods 165

4.3.1 Descriptive Analysis 165

4.3.2 Panel Data Approach 165

4.3.3 SEM Approach 166

4.3.4 Times Series Data using ARDL Approach 168

4.4 Sources of Data and Definition of Variables 172

4.4.1 Sources of Data 172

4.4.2 Definition of Variables 173

4.4.2.1 Economic Growth 173

4.4.2.2 Investment 173

4.4.2.3 Human Capital 174

4.4.2.4 Initial Income 175

4.4.2.5 Corruption 175

4.4.2.6 Foreign Aid 176

4.4.2.7 Education 176

4.4.2.8 Inflation 177

4.4.2.9 Poverty 177

4.5 Sample Size and the Problem of Missing Data 178

4.6 Data Transformation using Disaggregation method 180
CHAPTER FIVE: RESULTS AND DISCUSSIONS

<table>
<thead>
<tr>
<th>Section</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.0</td>
<td>Introduction</td>
<td>182</td>
</tr>
<tr>
<td>5.1</td>
<td>Data Processors</td>
<td>182</td>
</tr>
<tr>
<td>5.2</td>
<td>Panel Data Analysis</td>
<td>182</td>
</tr>
<tr>
<td>5.2.1</td>
<td>Spearman Rank-Order and Correlation Analysis</td>
<td>182</td>
</tr>
<tr>
<td>5.3</td>
<td>SEM Analysis</td>
<td>184</td>
</tr>
<tr>
<td>5.3.1</td>
<td>SEM Estimates for Base Sample using 3SLS</td>
<td>184</td>
</tr>
<tr>
<td>5.3.2</td>
<td>SEM Estimates for Base Sample using OLS Method</td>
<td>185</td>
</tr>
<tr>
<td>5.3.3</td>
<td>SEM Estimates for Base Sample using SURE Method</td>
<td>187</td>
</tr>
<tr>
<td></td>
<td>5.3.3.1 Growth as the Dependent Variable</td>
<td>188</td>
</tr>
<tr>
<td></td>
<td>5.3.3.2 Investment as the Dependent Variable</td>
<td>192</td>
</tr>
<tr>
<td></td>
<td>5.3.3.3 Human Capital as the Dependent Variable</td>
<td>194</td>
</tr>
<tr>
<td></td>
<td>5.3.3.4 Summary of the Results from SEM Analysis</td>
<td>196</td>
</tr>
<tr>
<td>5.3.4</td>
<td>Comparing the Results of 3SLS, OLS and SURE Methods</td>
<td>197</td>
</tr>
<tr>
<td>5.4</td>
<td>OLS Estimates for Topmost and Least Recipient Countries</td>
<td>198</td>
</tr>
<tr>
<td>5.5</td>
<td>ARDL Estimates on Corruption-Aid Model for</td>
<td></td>
</tr>
<tr>
<td></td>
<td>the Selected AMCs</td>
<td>203</td>
</tr>
<tr>
<td>5.5.1</td>
<td>ARDL Estimates for Morocco</td>
<td>204</td>
</tr>
<tr>
<td>5.5.2</td>
<td>ARDL Estimates for Egypt</td>
<td>208</td>
</tr>
<tr>
<td>5.5.3</td>
<td>ARDL Estimates for Tunisia</td>
<td>211</td>
</tr>
<tr>
<td>5.5.4</td>
<td>ARDL Estimates for Senegal</td>
<td>214</td>
</tr>
<tr>
<td>5.5.5</td>
<td>ARDL Estimates for the Special case (Nigeria)</td>
<td>217</td>
</tr>
</tbody>
</table>
CHAPTER SIX: CONCLUSION AND RECOMMENDATION

6.0 Introduction 226
6.1 Conclusion 226
6.1.1 Theoretical Contributions 227
6.1.2 Methodological Contributions 229
6.1.3 Empirical Contributions 230
6.1.4 Policy Implications 232
6.1.5 Scope and Limitations 235
6.2 Recommendation 236

REFERENCES 243

APPENDICES 257
# LIST OF APPENDICES

<table>
<thead>
<tr>
<th>Appendix</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Appendix A</td>
<td>IDB Member Countries and Date of Membership</td>
<td>257</td>
</tr>
<tr>
<td>Appendix B</td>
<td>Cumulative Development Assistance of IDB to AMCs from 1976-2010 (values in US$ m)</td>
<td>260</td>
</tr>
<tr>
<td>Appendix C</td>
<td>Socio-Economic Indicators of IDB Member Countries</td>
<td>261</td>
</tr>
<tr>
<td>Appendix D</td>
<td>Countries in the Muslim World</td>
<td>262</td>
</tr>
<tr>
<td>Appendix E</td>
<td>Least Developed Member Countries (LDMCs) as Per IDB Classification (Human Development Indicators for 2005)</td>
<td>263</td>
</tr>
<tr>
<td>Appendix F</td>
<td>The 34 Member Countries of OECD</td>
<td>264</td>
</tr>
<tr>
<td>Appendix G</td>
<td>List of Multilateral Aid Donors and UN Agencies</td>
<td>265</td>
</tr>
<tr>
<td>Appendix H</td>
<td>Descriptive Analysis for the Major variables (1987-2010)</td>
<td>266</td>
</tr>
<tr>
<td>Appendix I</td>
<td>Detail Results of Three-Stage Least Squares</td>
<td>267</td>
</tr>
<tr>
<td>Appendix J</td>
<td>Detail Results of Ordinary Least Squares</td>
<td>268</td>
</tr>
<tr>
<td>Appendix K</td>
<td>Detail Results of Seemingly Unrelated Regressions</td>
<td>269</td>
</tr>
<tr>
<td>Appendix L</td>
<td>Detail Results of OLS for Hypothesis 4</td>
<td>270</td>
</tr>
<tr>
<td>Appendix M</td>
<td>ARDL Results (Aid as Dependent Variable)-Morocco Diagnostic Test Results-Morocco</td>
<td>271</td>
</tr>
<tr>
<td>Appendix N</td>
<td>ARDL Results (Aid as Dependent Variable)-Egypt Diagnostic Test Results-Egypt</td>
<td>272</td>
</tr>
<tr>
<td>Appendix O</td>
<td>ARDL Results (Aid as Dependent Variable)-Tunisia Diagnostic Test Results-Tunisia</td>
<td>273</td>
</tr>
</tbody>
</table>
Appendix P: ARDL Results (Aid as Dependent Variable)-Senegal 274
Diagnostic Test Results-Senegal 274

Appendix Q: ARDL Results (Aid as Dependent Variable)-Nigeria 275
Diagnostic Test Results-Nigeria 275

Appendix R: Detail Results of ARDL Estimates for Morocco 276

Appendix S: Detail Results of ARDL Estimates for Egypt 286

Appendix T: Detail Results of ARDL Estimates for Tunisia 296

Appendix U: Detail Results of ARDL Estimates for Senegal 309

Appendix V: Detail Results of ARDL Estimates for Nigeria 317

Appendix W: Sample of Developmental Project by the IDB in Africa 328
<table>
<thead>
<tr>
<th>Table</th>
<th>Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Table 1.1</td>
<td>Similarities and Differences between Foreign Aid in OECD and IDB</td>
<td>18</td>
</tr>
<tr>
<td>Table 1.2</td>
<td>Human Development Index for AMCs (2010)</td>
<td>34</td>
</tr>
<tr>
<td>Table 1.3</td>
<td>Basic Indicators for AMCs (2010)</td>
<td>38</td>
</tr>
<tr>
<td>Table 2.1</td>
<td>Some Major Works on Aid-Growth Nexus</td>
<td>60</td>
</tr>
<tr>
<td>Table 3.1</td>
<td>Poverty-Intensity of Deprivation in AMCs (2010)</td>
<td>86</td>
</tr>
<tr>
<td>Table 3.2</td>
<td>Corruption Perceptions Index for AMCs (2010 &amp; 2011)</td>
<td>94</td>
</tr>
<tr>
<td>Table 3.3</td>
<td>Aid Disbursements, Grant Composition and Distribution in Africa (1975-2004)</td>
<td>104</td>
</tr>
<tr>
<td>Table 3.4</td>
<td>Summary of Figures on Total Aid to Africa</td>
<td>105</td>
</tr>
<tr>
<td>Table 3.5</td>
<td>The Major Shareholders of IDB</td>
<td>110</td>
</tr>
<tr>
<td>Table 3.6</td>
<td>Cumulative Development Assistance of IDB to Member countries from 1976-2010 values in US$ m</td>
<td>114</td>
</tr>
<tr>
<td>Table 3.7</td>
<td>Cumulative Development Assistance of IDB to Member Countries in Africa from 1976-2010 values in US$ m</td>
<td>121</td>
</tr>
<tr>
<td>Table 4.1</td>
<td>Definition of Variables and Sources of Data</td>
<td>172</td>
</tr>
<tr>
<td>Table 5.1</td>
<td>Spearman Rank-Order and Correlation Analysis (1987-2010)</td>
<td>183</td>
</tr>
<tr>
<td>Table 5.2</td>
<td>Pooled OLS Regression Estimates for Growth</td>
<td>186</td>
</tr>
<tr>
<td>Table 5.3</td>
<td>Panel Result with Growth as Dependent Variable</td>
<td>189</td>
</tr>
<tr>
<td>Table 5.4</td>
<td>Panel Result with Investment as Dependent Variable</td>
<td>193</td>
</tr>
</tbody>
</table>
Table 5.5: Panel Result with Human Capital as Dependent Variable 195
Table 5.6: Comparison of the Results for 3SLS, OLS and SURE Methods 197
Table 5.7: Impacts of AID in Topmost and Least Recipient Countries 200
Table 5.8: Unit Root Test (Morocco) 205
Table 5.9: Bound Test Results (Morocco) 206
Table 5.10: Granger-Causality Test (Morocco) 206
Table 5.11: Unit Root Test (Egypt) 208
Table 5.12: Bound Test Results (Egypt) 209
Table 5.13: Granger-Causality Results (Egypt) 210
Table 5.14: Unit Root Test (Tunisia) 211
Table 5.15: Bound Test Results (Tunisia) 212
Table 5.16: Granger-Causality Test (Tunisia) 213
Table 5.17: Unit Root Test (Senegal) 214
Table 5.18: Bound Test Results (Senegal) 215
Table 5.19: Granger-Causality Test (Senegal) 215
Table 5.20: Unit Root Test (Nigeria) 218
Table 5.21: Bound Test Results (Nigeria) 219
Table 5.22: Granger-Causality Test (Nigeria) 219
Table 5.23: Summary of Results on Granger-Causality Tests 222
# LIST OF FIGURES

<table>
<thead>
<tr>
<th>Figure</th>
<th>Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1</td>
<td>The Political-Geography of Africa</td>
<td>8</td>
</tr>
<tr>
<td>1.2</td>
<td>The Four Major Categorization of DA in IDB</td>
<td>29</td>
</tr>
<tr>
<td>2.1</td>
<td>The Theoretical Framework for this Study</td>
<td>48</td>
</tr>
<tr>
<td>3.1</td>
<td>Macro-Determinants of Poverty</td>
<td>88</td>
</tr>
<tr>
<td>3.2</td>
<td>ODA Distribution from 1970-2006</td>
<td>107</td>
</tr>
<tr>
<td>3.3</td>
<td>The Five Best Practice Dimensions</td>
<td>128</td>
</tr>
<tr>
<td>3.4</td>
<td>Four Fundamental Principles of Multilateral Aid</td>
<td>131</td>
</tr>
<tr>
<td>4.1</td>
<td>The Methodological Derivation of the Research Sample</td>
<td>148</td>
</tr>
</tbody>
</table>
**LIST OF ABBREVIATIONS**

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>AfDB</td>
<td>African Development Bank</td>
</tr>
<tr>
<td>AsDB</td>
<td>Asian Development Bank</td>
</tr>
<tr>
<td>APF</td>
<td>African Partnership Forum</td>
</tr>
<tr>
<td>AMCs</td>
<td>African Muslim Countries</td>
</tr>
<tr>
<td>ARDL</td>
<td>Autoregressive Distributed Lag</td>
</tr>
<tr>
<td>ASEAN</td>
<td>Association of South-East Asia Nations</td>
</tr>
<tr>
<td>AU</td>
<td>African Union</td>
</tr>
<tr>
<td>CIDA</td>
<td>Canadian International Development Agency</td>
</tr>
<tr>
<td>CPI</td>
<td>Corruption Perceptions Index</td>
</tr>
<tr>
<td>DA</td>
<td>Development Assistance</td>
</tr>
<tr>
<td>DAC</td>
<td>Development Assistance Committee</td>
</tr>
<tr>
<td>DFID</td>
<td>Department for International Development</td>
</tr>
<tr>
<td>DRC</td>
<td>Democratic Republic of Congo</td>
</tr>
<tr>
<td>ECM</td>
<td>Error Correction Model</td>
</tr>
<tr>
<td>FDI</td>
<td>Foreign Direct Investment</td>
</tr>
<tr>
<td>GMM</td>
<td>Generalized Method of Moments</td>
</tr>
<tr>
<td>H</td>
<td>Hijrah (Islamic calendar)</td>
</tr>
<tr>
<td>HCD</td>
<td>Human Capital Development</td>
</tr>
<tr>
<td>HDI</td>
<td>Human Development Index</td>
</tr>
<tr>
<td>HIPC(s)</td>
<td>Highly Indebted Poor Countries</td>
</tr>
<tr>
<td>ICOR</td>
<td>Incremental Capital-Output Ratio</td>
</tr>
<tr>
<td>IDB</td>
<td>Islamic Development Bank</td>
</tr>
</tbody>
</table>
LDCs: Less Developed Countries
LDMCs: Least Developed Member Countries
LICs: Low-Income Countries
LSDV: Least Squares Dummy Variable
MDGs: Millennium Development Goals
MFIs: Multilateral Financial Institutions
NEPAD: New Partnership for Africa’s Development
ODA: Official Development Assistance
OECD: Organization for Economic Cooperation and Development
OIC: Organization of the Islamic Conference
OLS: Ordinary Least Squares
OPEC: Organization of Petroleum Exporting Countries
SEM: Simultaneous Equations Model
SPDA: Special Program for the Development of Africa
SSA: Sub-Saharan Africa
SURE: Seemingly Unrelated Regressions Estimate
SWAPs: Sector-Wide Approaches
TNCs: Trans-National Corporations
TVSD: Technical and Vocational Skills Development
UNDP: United Nations Development Program
USAID: United States Agency for International Development
2SLS: Two-Stage Least Squares
3SLS: Three-Stage Least Squares
CHAPTER ONE

INTRODUCTION

1.0 Introduction

This section presents the general introduction on the subject matter of our study, which is meant to serve as a general overview. Hence, issues such as background of the study, problem statement, research questions and objectives of the study are discussed. In the same vein, other important issues like significance of the study, conceptual framework and the overall organization of the entire thesis are presented and discussed to set the ball rolling for more elaborate and detail study.

1.1 Background of the Study

It has been acknowledged by numerous writers and scholars that Africa is perhaps the richest continent in the world in terms of natural, mineral and human resource endowments. Hence, Africa prides with important world reserves like 10 percent in oil, 40 percent in gold, 80 percent in chrome and as much as 90 percent in the platinum metals. In fact, it has been noted that the potentials of the continent is vast. The continent as at August 2012 has 54 countries (including the newly created South Sudan) and prides with a population of 1.031 billion people. Nonetheless, the African continent contains the largest number of backward and least developed countries, while almost half of its population lives in poverty. Among the least developed countries of 48 identified by the United Nations Development Program (UNDP) - Human Development Report of 1998, 32 are African countries. Also, 34 African countries are among the 45 lowest-ranked countries and the Human Development Index (HDI) for Sub-Saharan Africa
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REFERENCES


253


