

## **IMF CONDITIONALITY: WHAT EFFECT ON THE LABOR MARKET?**

Mina Makboul<sup>1</sup> and Otmane Sayih<sup>2</sup>

<sup>1</sup>Professor of Higher Education at Hassan II University, Faculty of Legal, Economic, and Social Sciences in Ain Sebaa, LARNED Laboratory, Casablanca, Morocco.

<sup>2</sup>PHD Student at Hassan II University, Faculty of Legal, Economic, and Social Sciences in Ain Sebaa, LARNED Laboratory, Casablanca, Morocco.

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### **ABSTRACT**

This article explores the multifaceted impact of IMF policies, particularly its conditionality measures, on economies and societies. Outcomes vary, including increased poverty and inequality alongside economic benefits. Labor market deregulation, promoting competitiveness but raising concerns for vulnerable workers and inequality, is also debated. In essence, IMF policies yield complex results, requiring individualized assessments. The article calls for further research to understand the specific influences of IMF conditionality on labor markets. This could provide insights into how policies like trade liberalization, privatization, and financial sector reform affect employment. It underscores the importance of considering contextual variations among countries when shaping future policies.

**Keywords:** Conditionality, Economic Growth, IMF, labor market.

### **Introduction**

The International Monetary Fund (IMF) holds a prominent place in the current global financial architecture (United Nations, 2023, p. 4) and plays a crucial role as a regulatory organization in the world economy. However, recent changes in the global economy have raised questions about the effectiveness of existing international organizations, including the IMF. For example, the Great Recession, which erupted in the United States, revealed the fragility of developed economies and highlighted the growing interconnectedness between national economies resulting from financial globalization (Anheier, 2013, p. 31). However, even if the success of the Bretton Woods system is often debated. Prominent scholars argue that the Bretton Woods Conference was one of the most successful economic achievements of the twentieth century (Eichengreen, 2008, p. 133; Margaret Garritsen De Vries, 1986, p. 4).

On the other hand, researchers such as (Copelovitch, 2010, p. 3) argue that the Fund has effectively been the lender of last resort in the international monetary system. For instance, between 1984 and 2003, the Fund disbursed over 400 billion U.S. dollars to countries facing balance of payments problems and financial crises. According to (Joyce, 2013, p. 140-141) the IMF generally plays the role of international lender of last resort and describes the justifications for the IMF's role as an international lender of last resort.

Consequently, to ensure the funds disbursed, the fund imposes requirements on its loans. This practice, known as conditionality (or mandated economic reform), along with other Fund practices, has been the subject of much criticism.

In this article, we will undertake a literature analysis regarding the IMF's conditionality and its influence on countries' macroeconomic indicators, with a specific focus on economic growth, and we will also explore its influence on the labor market. The core question at the heart of this article is as follows:

### **What is the effect of IMF conditionality on the labor market?**

#### **IMF Reforms and the Concept of Conditionality:**

The economic reforms of the IMF are designed to shift power from government to market actors in order to solve a country's structural problems, which impede economic growth and development (Abouharb & Cingranelli, 2008, p. 1; Blanton et al., 2015, p. 2; Vreeland, 2002, p. 122). These reforms include a wide range of economic policies aimed at reducing public spending, privatizing state-owned enterprises, removing trade and capital mobility barriers, and increasing labor market flexibility (Stiglitz, 2002, p. 56, 96). The objective behind these reforms is that economic liberalization has positive effects on several macroeconomic indicators as well as wealth (FRANKEL & ROMER, 1999, p. 379-380; Salinas & Aksoy, 2006, p. 25; Wacziarg & Welch, 2008, p. 188).

At the same time, the conditions imposed by the IMF pushed governments to cut expenditures in order to reduce debts and deficits. Most governments under IMF programs choose to cut spending on butter rather than weapons, as security concerns often outweigh social welfare concerns. (Mark et al., 2021, p. 3). Generally, when governments implement austerity policies, the actual implementation often results in spending cuts allocated to education, healthcare, and social safety nets.

#### **IMF Conditionality and Economic Growth:**

The IMF's conditionality has been widely studied to assess its influence on macroeconomic indicators such as balance of payments, economic growth, inflation, and other indicators. The

results of these research efforts have consistently diverged. Let's use economic growth as an example to further illustrate the outcomes of studies conducted on IMF conditionality.

Two studies have shown no significant effect on economic growth. The first is a before-and-after study by (Pastor, 1987, p. 254,258) conducted in 18 Latin American countries, covering the period 1965-1981. The second study is conducted by (Atoyan & Conway, 2006, p. 100), who employed a methodological approach combining with-without and instrumental variables to study 95 developing countries from 1993 to 2002. (Atoyan & Conway, 2006, p. 100) include all different IMF lending arrangements and conclude that « IMF programs do not statistically improve real economic growth in participating countries, but there is stronger evidence of improved economic growth in the years following a program » (Atoyan & Conway, 2006, p. 99).

(Dicks-Mireaux et al., 2000, p. 495,521) conducted a study on 74 low-income countries participating in IMF arrangements from 1986 to 1991, and found statistically significant results showing an increase in economic growth.

The before-and-after study by (Killick et al., 1990) covering the period 1975-1985 and the regression-based study by (Conway, 1994) on 74 developing countries, from 1976 to 1986, show a short-term negative effect on growth and an improvement in the longer term after three and two years.

The study by (Przeworski & Vreeland, 2000, p. 389) also employs on a regression-based approach, studying 135 countries from 1951 to 1990, giving 4216 country-years. The results of their study are as follows: « Our results indicate that countries that do not enter into IMF programs grow faster than those that do even when both groups face high domestic deficits or foreign reserves crises » (Przeworski & Vreeland, 2000, p. 403).

Another regression-based study was conducted by (Butkiewicz & Yanikkaya, 2005, p. 376-377), who examined the long-term growth rates of 100 developing countries from 1970 to 1999. This study demonstrates a significant negative effect of IMF loans on public and private investment growth. The authors also emphasize that IMF policy conditions require reductions in public spending, and the first cut is typically made in public investments, which has negative effects on overall investments and growth in a country. They also mention that the larger the loans supported by the Fund, the greater the economic problems of the participating countries.

(Barro & Lee, 2005), who conducted a study using an instrumental variables approach to examine 130 countries from 1975 to 2000, arrive to the conclusion of a negative effect on economic growth. Furthermore, they emphasize that the negative effect is proportionate to the amount of IMF loans (Barro & Lee, 2005, p. 1263).

The results of the various studies published are mixed. There has been no clear consensus among researchers on the effects on economic growth, but (Vreeland, 2007, p. 122) asserts that the emerging consensus is that IMF arrangements harm economic growth. The most recent studies, which show statistically significant results of negative effects on economic growth, use more sophisticated and advanced methodological approaches.

### **IMF Conditionality and the Labor Market**

IMF-imposed conditionality significantly impacts the living conditions of the poorest populations and contributes to the exacerbation of poverty, as evidenced by a large body of literature (Abouharb&Cingranelli, 2008, p. 31; Kentikelenis et al., 2016, p. 8; Nooruddin & Vreeland, 2010, p. 14; Oberdabernig, 2013, p. 114). Previous studies have also linked IMF reforms to inequality, poor health and education outcomes, women's rights violations, and increased government repression (Abouharb&Cingranelli, 2008, p. 50-55, 2009, p. 50; Detraz & Peksen, 2016, p. 83; Kentikelenis et al., 2016, p. 8; Oberdabernig, 2013, p. 114). Additionally, IMF reforms often encourage countries to create export processing zones (EPZs), which benefit from exemptions from national labor laws. It has been shown that labor rights violations are more significant in EPZs compared to non-EPZ areas (Abouharb&Cingranelli, 2008, p. 123).

Often, a country under IMF agreement is obliged to reduce its budget deficit, which can be achieved by increasing tax revenues or reducing public spending. The redistributive effects of these reforms depend on the fiscal policy implemented by the government. Generally, reductions in public expenditures entail cuts in social spending, public sector wages, and public sector employment. The resulting increase in unemployment and decrease in wages in this sector tend to raise poverty levels and worsen income distribution (Oberdabernig, 2013, p. 114).

There is a consensus in the literature that the Fund has pushed governments to deregulate labor markets, often through explicit labor market conditionality (Blanton et al., 2015; Gunaydin, 2018). According to (Burgess, 2010, p. 213-220) many of the labor policy conditions formulated by the IMF target labor market flexibility - laws governing employment contracts, working conditions and hiring and firing provisions. Programs including labor market conditions accounted for approximately 44 percent of all IMF programs in 1999 (Caraway et al., 2012, p. 30).

In general, both the World Bank and the IMF have promoted reforms calling for greater labor flexibility, which is often seen as necessary for a viable and competitive economy (Blanton et al., 2015, p. 3; Gunaydin, 2018, p. 3). However, according to economists within the IMF (Alvadero et autres 2013), greater flexibility can pose challenges for workers, especially those with limited

skills, and hence play an important role in explaining inequality developments (Dabla-Norris et al., 2015, p. 33).

### **Conclusion**

IMF policies have a complex impact on populations, with nuanced results. Some studies have reported negative effects, such as increased poverty and inequality, but it should be noted that outcomes depend on how these policies are implemented by national governments. Additionally, IMF reforms can encourage the creation of export processing zones, which have economic benefits but also present challenges in terms of labor rights. Labor market deregulation is also debated, with benefits for competitiveness, but also concerns about its impact on less-skilled workers and inequality. In summary, the impact of IMF policies is complex and depends on a variety of factors, requiring case-by-case assessment.

Future research could delve into the analysis of specific elements of IMF conditionality and their influence on the labor market. This would enable a better understanding of how particular policies, such as trade liberalization, privatization of state-owned enterprises and financial sector liberalization, have specific effects on employment and job creation. Such an approach would also make it possible to assess how these policies may vary from one country to another according to their economic and institutional contexts, providing valuable insights to guide future policies.

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