4

IMPACT OF IMF FINANCING[20]

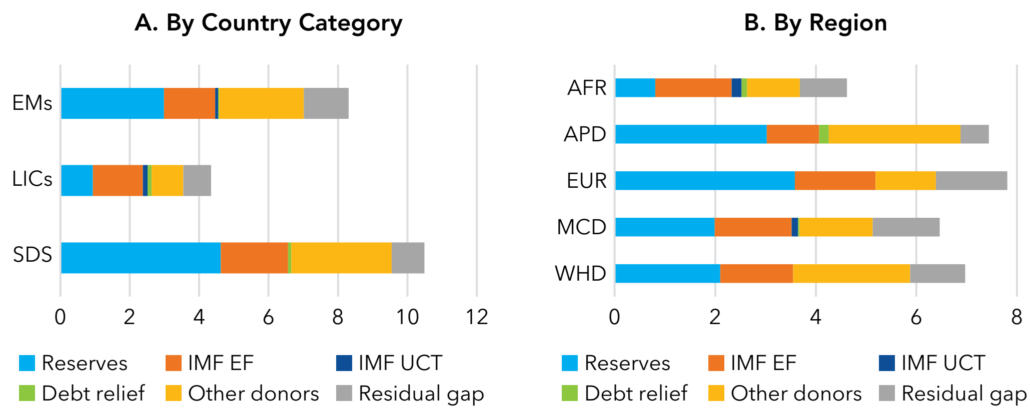
Roadmap. This section provides evidence on the role of Fund financing in addressing BOP financing needs (Section IV.A), marshaling financing from other sources such as other official agencies and private capital markets (Section IV.B), and mitigating output losses (Section IV.C), followed by an assessment of the overall impact of Fund financing (Section IV.D).

A. ROLE OF FUND SUPPORT IN ADDRESSING BOP FINANCING NEEDS

Role of Fund financing in addressing BOP needs. Fund decisions on lending are based on assessments of a country's BOP needs at the time of approval, taking account of policies the country has taken or is planning to take to address its economic situation. Documents supporting all requests for use of Fund resources are required to present estimates of financing (and fiscal) needs and how such needs are to be met, including through Fund credits.[21]

Expected role of Fund financing. At the time of the approval of Fund financing (EF and UCT arrangements) in 2020, the average ex ante financing gap in EMs was about 8 percent of GDP. The Fund contributed about 1 percent of GDP toward closing this gap, with other sources of financing (about 2 percent of GDP) and reserve drawdowns (about 2½ percent of GDP) making up much of the rest (Figure 18). In LICs, the Fund's share was expected to be proportionately larger, contributing about 1 percent of GDP toward closing an average financing gap of slightly

FIGURE 18. EX ANTE IMF FINANCING RELATIVE TO OTHER SOURCES, 2020
(In percent of GDP)



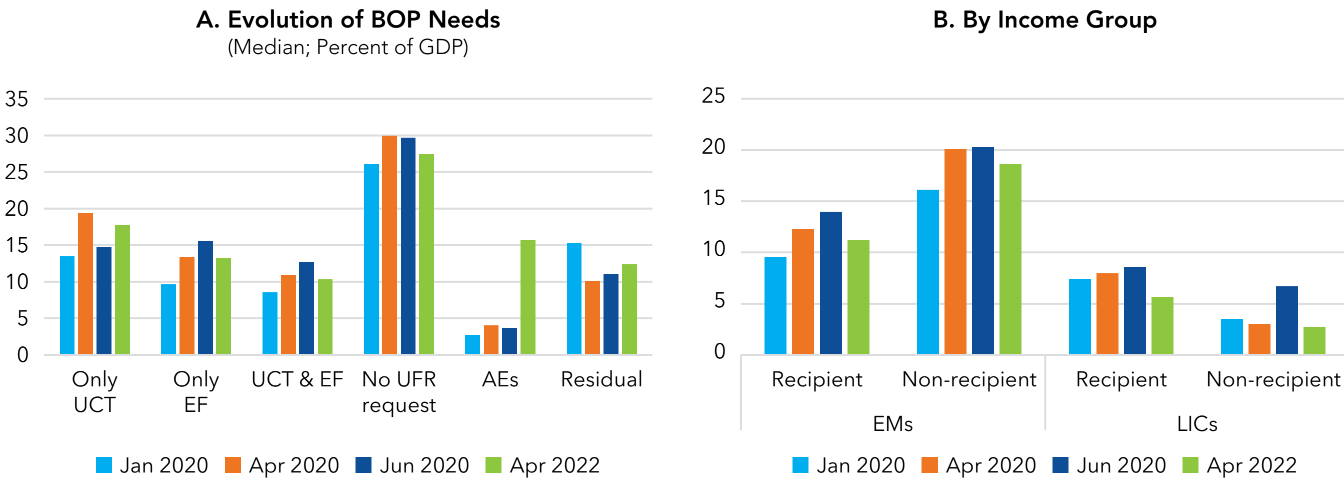
Source: Batini and Li (2023).
Note: Other identified sources include financings from the World Bank. UCT arrangements for Sudan and Somalia are excluded because they received extremely large HIPC debt relief relative to BOP gaps.

[20] This section draws on background papers by Batini and Li (2023), Koh and Wojnilower (2023), and Ocampo and others (2023).

[21] Note that, unlike for UCT arrangements, in the case of UFR documents supporting RCF/RFI drawings, some financing to meet BOP needs may remain unidentified.

FIGURE 19. EVOLUTION OF 2020 BOP NEEDS BY FUND FINANCING AND INCOME GROUP

(Median; in percent of GDP)



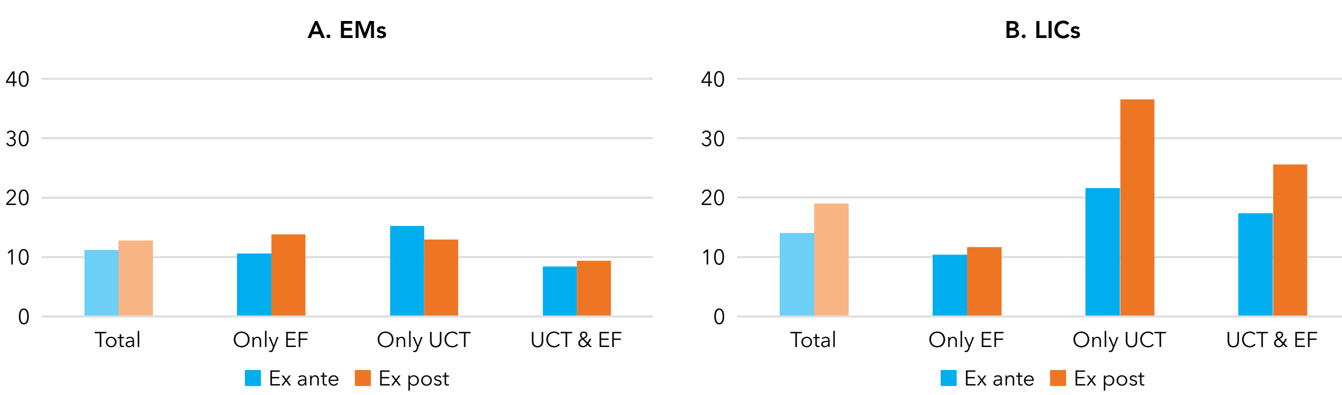
Source: Batini and Li (2023).

over 4 percent of GDP, with other financing sources and reserve drawdowns each playing a roughly similar role. For small developing states in particular (which span middle-income countries and LICs), the IMF's share was relatively low as the anticipated gap for these countries averaged over 10 percent of GDP, reflecting their greater vulnerability to the pandemic. Looked at by region, the role of Fund financing was more significant relative to other sources in the African region than elsewhere.

From ex ante to ex post developments. The Fund's decisions on lending are, by necessity, based on its best estimates of the financing needs at the time that the country's financing request is being considered. These estimates require judgments about developments that are difficult to forecast accurately, such as autonomous capital flows and financing disbursed by other donors. Hence, ex post, BOP needs can differ from initial estimates and the Fund may end up financing a larger or smaller share of the financing gap than it had envisaged. Nevertheless, for countries that requested Fund financing, the ex-post values of BOP needs (using April 2022 WEO data) turned out generally close to albeit a little below the initial 2020 estimates (using April 2020 WEO data), though with some variation among income groups and among countries based on the kind of Fund financing they accessed or did not access (Figure 19).

FIGURE 20. EX ANTE VS. EX POST SHARE OF FUND FINANCING OF BOP NEEDS, 2020

(In percent)



Source: Batini and Li (2023).

Note: Ex ante shares of Fund financing to total financing needs are calculated based on data from the April 2020 WEO, while ex post shares are calculated based on data from the April 2022 WEO.

Ex-post share of Fund financing. For EMs, the Fund ended up financing, on average, roughly the share of BOP needs envisaged ex ante. For countries receiving EF the ex-post share was a bit higher than the 10 percent ex-ante share, while for countries receiving only UCT the ex-post share of 15 percent was somewhat higher than initial estimates. For LICs, the picture is different. While in countries receiving only EF there was little difference between ex-post and ex-ante shares, countries receiving only UCT ended up with nearly 40 percent of their BOP needs met by Fund financing, nearly twice the ex-ante share, and countries receiving both EF and UCT had about 25 percent of needs met, also considerably higher than expected (Figure 20).

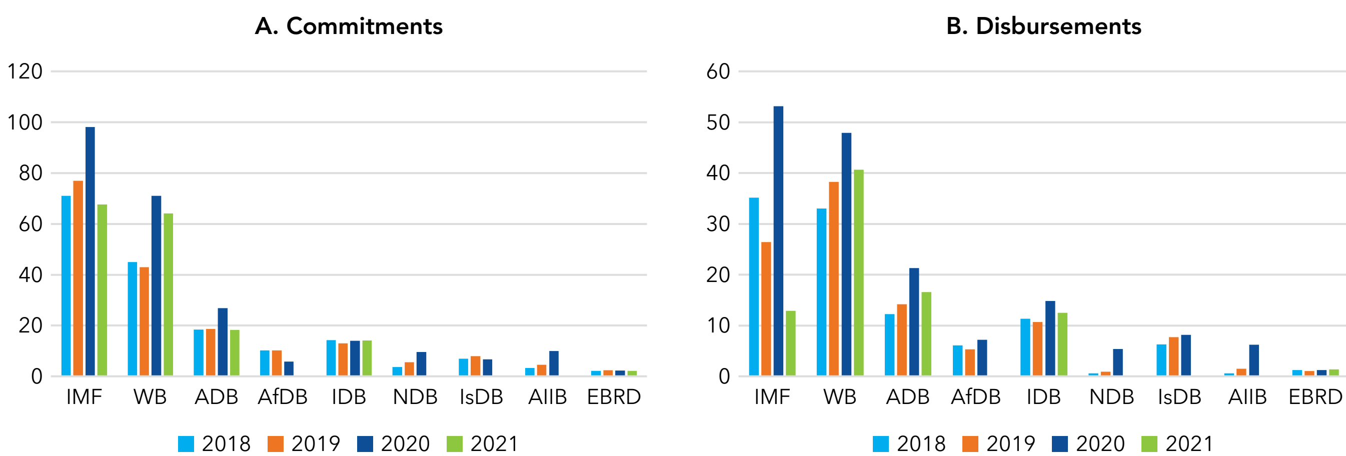
B. MARSHALLING SUPPORT FROM OTHER SOURCES

Collaboration with Partners

Fund support as part of a package. The Fund's support for a country can help meet financing needs in several ways beyond the financing it provides directly. First, when considering a country's request for support, the IMF provides an estimate of the country's BOP gap and of the fiscal financing gap—which are useful to other partners as measures of the extent of help that a country needs—and works with other potential lenders to identify ways of filling the gap. Second, the signal provided by the provision of Fund financing, and/or the Fund's positive assessment of a country's macroeconomic framework and policies, can help unlock funding from other official sources. Third, the Fund's support can have a catalytic effect on private capital flows, again because of reassurance of availability of financing and quality of the policy framework. Fourth, the Fund works with official partners (for example, G20, Paris Club) to mobilize debt relief, and, if necessary, debt treatments, to ease financing gaps.

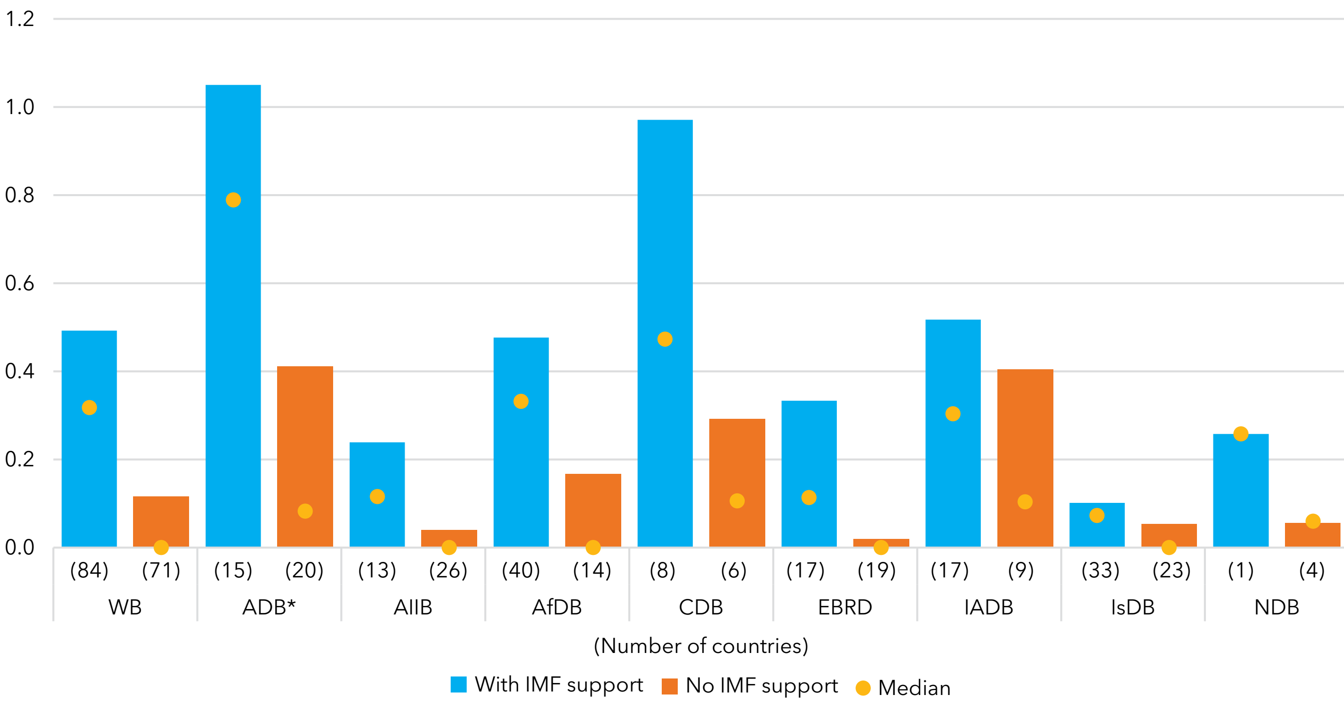
Financing by the Fund and multilateral development banks (MDBs). Alongside the Fund, MDBs provided important additional financial support in 2020–21, with total commitments of around $145 billion and disbursements of around $112 billion in 2020 (Figure 21). Of course, not all of this financing was directly related to the COVID-19 pandemic: some of this financing corresponded to ordinary operations that had already been approved before the pandemic and some corresponded to new operations that would have been approved and disbursed even in the absence of COVID-19. That said, the additional support is evident from the large increase of 40 percent in aggregate MDB financial commitments and of 33 percent in disbursements in 2020. Among MDBs, the World Bank accounted for 70 percent ($28 billion out of $41 billion) of the increase in MDB commitments and 30 percent ($10 billion out of $33 billion) of the increase in MDB disbursements in 2020.

FIGURE 21. OFFICIAL LENDING: IMF AND OTHER MULTILATERAL LENDERS
(In USD billions)



Sources: Ocampo and others (2023); IEO calculations using data from IMF and World Bank and other MDBs.
Note: Financing includes all total commitments/total disbursements to sovereign (not just strictly COVID-19-related). FCL and PLL are included in total IMF financing.

FIGURE 22. COVID-19 FINANCIAL COMMITMENTS TO EMDEs BY SELECTED MDBs
(In percent of GDP)



Source: Ocampo and others (2023).
* Excludes six outliers that distort the average.

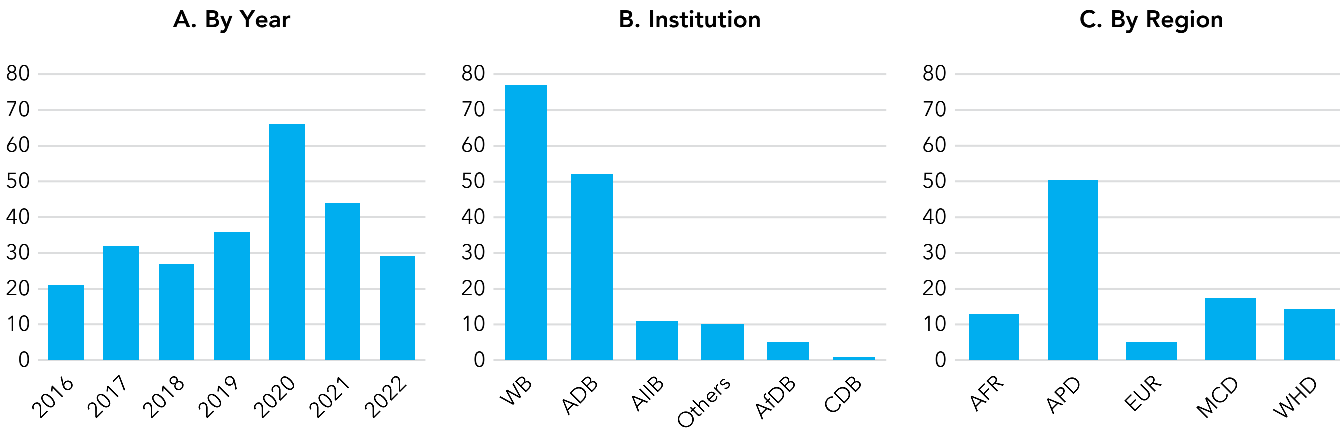
Relationship between Fund support and MDB financing. Fund and MDB support tended to go hand in hand. Average COVID-related financial commitments to EMDEs from other official institutions, including the World Bank, were substantially higher for countries that received Fund support than in cases of no Fund support, across the spectrum of MDBs (Figure 22).

Provision of assessment letters. The Fund collaborated with many of these multilateral agencies during the pandemic, typically at the level of country teams working in different institutions. As reported in the country case studies, cooperation and information exchange at the team level was generally good, although on occasions there were difficulties in receiving information on likely financing from different institutions. There was also a substantial pick-up in the volume of assessment letters provided by the IMF, which provide assurance to other lenders about a country's macroeconomic framework (Figure 23). Most letters were provided at the request of the World Bank and Asian Development Bank (ADB), but letters were also provided to newer agencies like the Asian Infrastructure Investment Bank (AIIB). The share of assessment letters by country was particularly high for EMDEs in Asia, which may reflect that these countries used Fund resources less than others. Interviews with staff at the ADB indicate that Fund staff were perceived as trying to provide letters in a "very timely manner" during the pandemic.

Collaboration with the World Bank. Over half of the EMDE member countries of the Bank and the Fund received COVID-related financial assistance from both institutions over March 2020-June 2021.[22] In another quarter of cases, neither institution provided financial support, reflecting either a lack of interest from the country or lack of access to financing from both institutions. Hence, in about 75 percent of countries, there was alignment between the provision of financing (or lack of it) between the two institutions (Figure 24). Moreover, as shown in Figure 22, Bank commitments for countries also receiving Fund support was substantially greater (about five times relative to GDP).

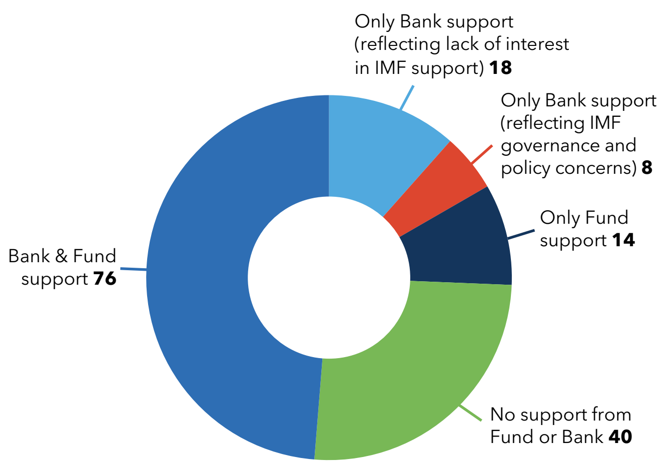
[22] COVID-related financial assistance includes all IMF financial support, and financial support for COVID-related lending from the World Bank based on data provided by the World Bank—see Ocampo and others (2023) for details on how COVID-related financial assistance was identified.

FIGURE 23. ASSESSMENT LETTERS PROVIDED BY THE IMF
(Number)



Source: Ocampo and others (2023).
Note: Some assessment letters were provided jointly to two institutions and are counted under both institutions in the middle and right-hand side charts but only counted once in the left-hand side chart.

FIGURE 24. FUND AND BANK COVID-19 FINANCIAL ASSISTANCE DISBURSED TO EMDEs, MARCH 2020–JUNE 2021
(Number of countries)



Source: Ocampo and others (2023).
Note: Ocampo and others (2023) explains the methodology used to identify disbursements of COVID-19 financial assistance for the two institutions.

Understanding deviations in alignment of IMF and World Bank support. In the remaining 40 cases, representing a quarter of the total, a country received COVID-related disbursements from one institution but not the other (14 received support only from the Fund, 26 only from the Bank) during the period covered by this analysis. There were a number of factors leading to these deviations:

- Stronger policy requirements for Bank disbursement. In six of the cases of Fund support without Bank support (Armenia, Cameroon, El Salvador, Guatemala, Madagascar, and Nigeria), the Bank approved COVID-19 financial assistance before the end of its fiscal year (which ends in June in the case of the Bank) but did not disburse it before June 2021. For example, in the case of Nigeria

(Christensen, Kayizzi-Mugerwa, and others, 2023), the financing approved was not disbursed by the Bank because the PA regarding the harmonization of Nigeria's exchange rate regime was not met.

- Later approvals of new Bank financial commitments. In another six countries (Angola, Chile, Guinea-Bissau, Somalia, South Africa, South Sudan), the difference arises because the Bank's COVID-19 financing was approved substantially later than Fund financing. For these cases, the new commitments related to the pandemic were approved only after June 2021.

- More flexibility in Bank financing. In 26 countries (8 LICs and 18 middle-income countries), the Bank provided COVID-related financial support, but the Fund did not. In 8 of these cases (4 LICs, 4 middle-income countries), the Bank provided support, notwithstanding issues related to debt sustainability, governance, and health policies that prevented the provision of Fund support, in some cases providing relatively small amount of humanitarian support based on highly concessional loans and grants. In the 18 other cases (4 LICs, 14 middle-income countries), there was no demand for Fund financing despite the demand for Bank financing, possibly due to concerns about stigma of borrowing from the Fund. Altogether, this suggests that the Bank may have benefitted from a more flexible set of lending instruments with less stigma to help countries address COVID-related issues. This appears especially true for middle-income countries, which represent 70 percent of the countries that only received Bank support.

Collaboration among Bank-Fund country teams. Both the IEO country case studies and those conducted by the World Bank's Independent Evaluation Group (IEG)[23] suggest that there was excellent technical collaboration during the pandemic between Bank and Fund country teams. This finding is supported by the fact that a large majority of respondents to our staff survey indicated that collaboration with the World Bank was intense or very intense. Two examples of countries where collaboration was rated as strong by either an IEO or IEG case study are Morocco and Serbia. The Bank's continued presence in the field was particularly useful to Fund staff in some instances to provide trusted information on local conditions such as the spread of the pandemic. However, country teams also reported that in some difficult cases they perceived a lack of agreement on the appropriate country strategy at the more senior levels of the two institutions. Indeed, nearly 40 percent of staff survey respondents felt that the coherence of approaches to financing between the two institutions was somewhat effective or not effective.[24] These differences contributed to tensions that could delay Fund financing and leave continued uncertainty about meeting BOP needs.[25]

Helping with Debt Burdens

Debt Service Suspension Initiative (DSSI). Following a joint call for action by the World Bank President and the IMF Managing Director for additional resources to bolster the crisis mitigation efforts of LICs, G20 Finance Ministers endorsed a DSSI covering official bilateral loans on April 15, 2020. The initiative, which was also supported by the Paris Club, Kuwait, and the UAE, covered 73 IDA-eligible and UN Least Developed Countries with debt service payments to the IMF and World Bank. Participating countries were encouraged to seek similar debt service relief from private creditors. In 2020, 43 countries benefited from US$5.7 billion in debt service suspension. The IMF and the World Bank also assisted beneficiaries of the DSSI to put in place a monitoring framework for their fiscal efforts in response to the COVID-19 crisis; the framework was endorsed by the G20 in June 2020 and developed and put in place soon thereafter.

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[23] The evidence comes from IEG's case studies conducted as part of the early-stage evaluation of the WBG's COVID-19 economic response (World Bank, 2023). The evaluation examined the Bank Group's early response to the crisis, defined as interventions over the 15 months of April 2020 through June 2021. Although the case studies cover the whole evaluation period, the portfolio analysis considers a subset of the evaluation period, from April 2020 to April 2021, based on Bank Group COVID-19 response data availability.

[24] The corresponding figure for other MDBs was over 50 percent, suggesting even greater issues with collaboration.

[25] For example, in one case where Fund staff had drafted its country report on assurances that Bank support would play a major complementary role to Fund financing, a late decision at the senior levels of the Bank to withdraw the assurances left Fund staff scrambling for alternatives to fill the gap. However, this did not disrupt the good relationships between the country teams.

Common Framework for Debt Treatments. A Common Framework for Debt Treatments beyond the DSSI was developed by the G20, with the Paris Club, the IMF, and World Bank, and agreed in November 2020 as a structure for guiding agreements on debt treatments for eligible countries. Requests for debt treatments by Chad, Ethiopia, and Zambia are now being processed under the Framework. However, progress was minimal during the evaluation period, in part because of different interests among creditors.

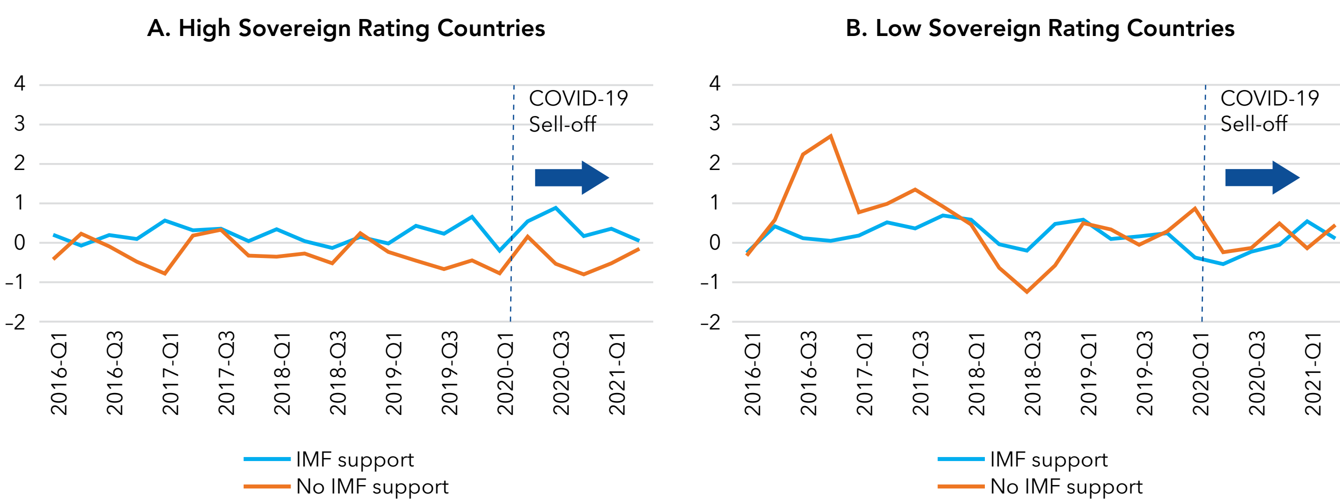
Catalytic Effect on Private Capital Flows

Seeking catalytic effects. Beyond providing direct support for a country's BOP needs, Fund financing can help relax countries' external constraints by increasing their net access to private sources of finance through a catalytic effect—as Fund financing provides assurances about a country's macroeconomic policies.[26] However, it is difficult to establish the catalytic effect of Fund financing in the best of circumstances given sample selection bias (countries with strong policies are less likely to need Fund financing). One common approach relies on comparing the behavior of capital flows in the "treatment" group (the group receiving financing) with that of a "control" group (similar countries that did not receive financing). However, the difficulties of finding an appropriate control group, or adequately controlling for other factors that may be affecting the two groups, make inference difficult. This was particularly so during the pandemic because there were many countries in the treatment group and few in the control group. Moreover, actions by the major central banks played a significant role in calming financial conditions and facilitating the resumption of capital flows, making it difficult to sort out the Fund's role. Given these difficulties, we use various data sources and cuts of the data to look for robust evidence of a catalytic effect of Fund financing.

High vs. low credit ratings. As a simple measure of the Fund's impact, we compare the behavior of net portfolio flows in EMDEs that received Fund financing and those that did not, looking separately at countries that have high credit ratings and those with low credit ratings (Figure 25). From this cut of the data, it is unclear whether Fund support had any impact on the pace at which net portfolio flows bounced back in mid-2020. In fact, a catalytic effect is harder to discern in the countries with a low credit rating—just those countries where in principle the IMF seal of approval should have the greatest catalytic value.

EMs vs. LICs. Splitting countries by income group also does not uncover much evidence of a possible catalytic

FIGURE 25. NET PORTFOLIO FLOWS BY SOVEREIGN RATING: ROLE OF FUND SUPPORT
(In percent of lagged GDP; median)



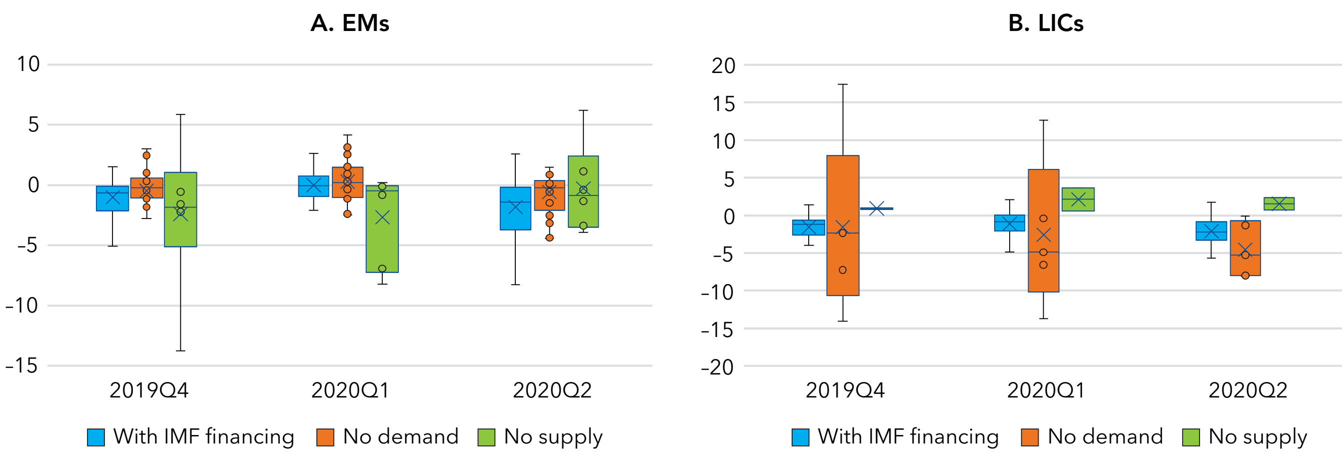
Source: Batini and Li (2023).
Note: Positive values indicate net inflows.

[26] In principle, such a catalytic effect is likely to be strongest for a UCT arrangement but may also occur for emergency financing given the ex-ante conditions that must be satisfied for such financing to be provided, including positive debt sustainability and capacity to repay assessments.

effect of Fund financing in 2020Q1-Q2. Data suggests that in median terms, there is little difference in net outflows between EMs that did not request Fund financing and those from EMs supported by the Fund. However, EMs with unmet requests experienced much larger outflows in net terms than the average EM. In the case of LICs, a different pattern emerges: the median (and average) LIC that requested but did not receive Fund financing experienced a net inflow of capital, while the median (and average) LIC that either received Fund support or did not ask for it both experienced capital outflows in net terms (Figure 26).

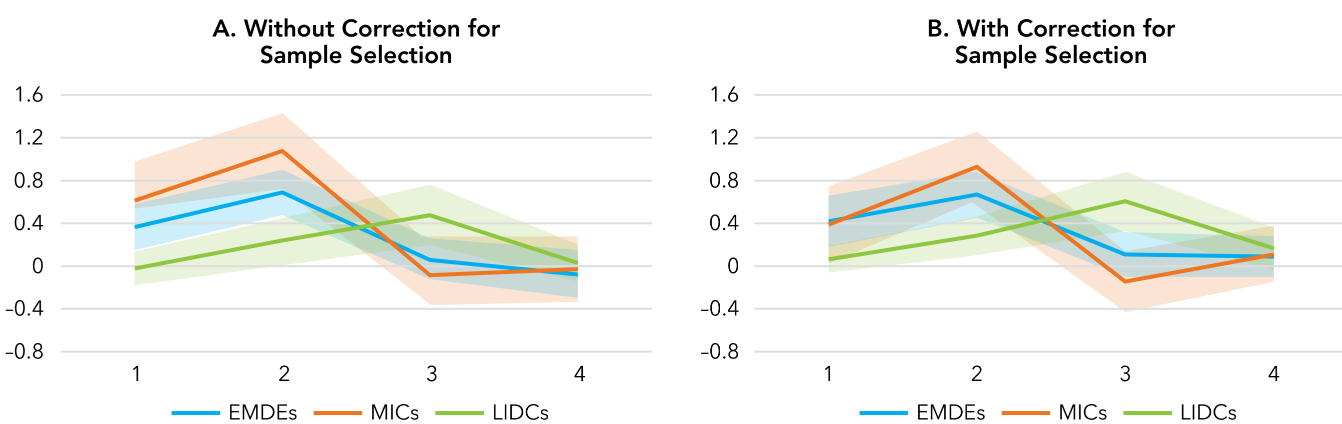
Adjusting for country characteristics. The above data need to be interpreted cautiously because of sample selection bias: countries that used Fund resources are likely to be those that suffered the greatest economic shock and the greatest difficulty sustaining access to international capital markets. To correct for this bias, we applied more sophisticated econometric techniques estimating the response of portfolio flows for a panel of 83 EMDEs over the period 2018–2021 (comprising 60 EMs and 23 LICs) using quarterly BOP data. This analysis uncovers somewhat more consistent evidence in favor of a catalytic effect of Fund financing, both when we estimate a simple fixed-effect panel model and when we correct for country characteristics using a covariance-balance propensity score (CBPS) approach (Figure 27). Once more the effect appears stronger for EMs than LICs both on impact and in the subsequent quarter, but also dissipates faster. These differences in the catalytic effect of Fund financing between middle-income and LICs may reflect different market perceptions with respect to Fund loans to these two groups, as well as the

FIGURE 26. IMF FINANCING AND NET PRIVATE CAPITAL FLOWS—EMs AND LICs
(In percent of GDP)



Source: Batini and Li (2023).

FIGURE 27. RESPONSE OF PORTFOLIO FLOWS TO FUND EMERGENCY FINANCING



Source: Batini and Li (2023).

differential impact of Fund financing in countries with different income fundamentals.

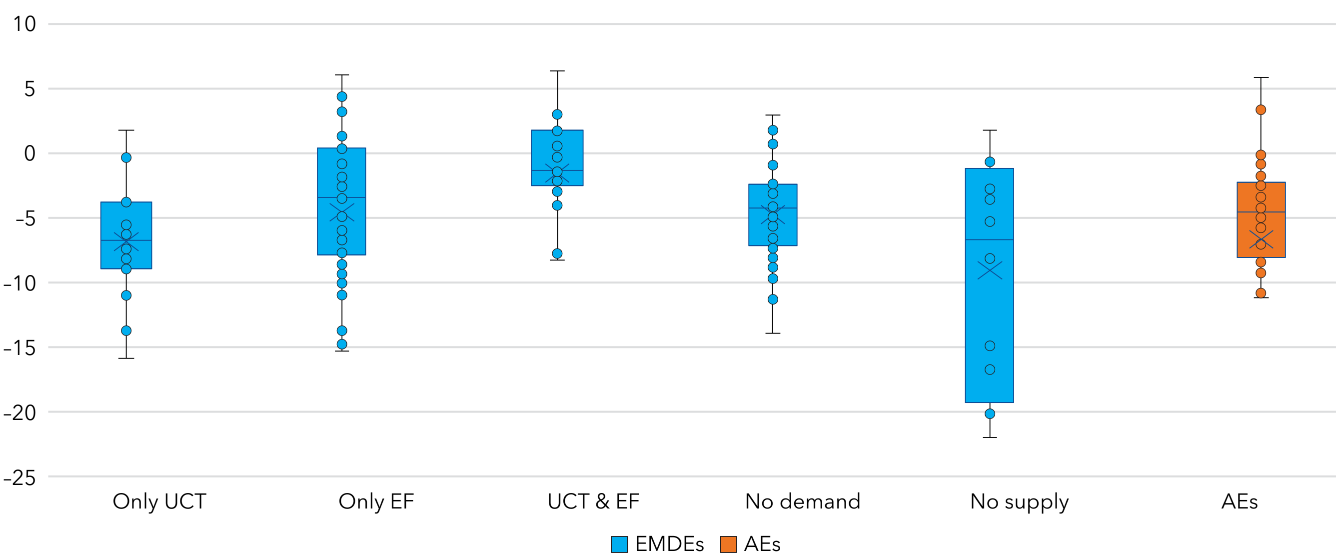
C. MITIGATING THE COVID-19 SHOCK

Impact on macroeconomic outcomes. Estimating the impact of Fund financing on macroeconomic outcomes is challenging, but it is important to make an attempt as financing is not an end in itself but intended to help mitigate economic losses. A first look at the data clearly shows differences in economic outcomes according to the support received from the Fund (Figure 28). In terms of real growth, on average countries that received emergency Fund financing (either in isolation or blended with UCT financing) experienced smaller contractions than countries that asked but did not receive financing. Moreover, the negative tail of outcomes experienced by countries that were unable to access Fund financing was more dispersed. Among recipients of Fund support, those which obtained a combination (either simultaneous or sequential) of emergency and UCT financing seemed to have fared better on average than all other groups, including those which never requested financing, outperforming AEs as well. In light of this, the fact that a very large share of EF recipients did not eventually shift to a UCT program points to a missed opportunity.

Explaining growth differences. The difference in growth performance was primarily related to the fact that, on average, private consumption in 2020 was weaker in countries that requested but were not provided with IMF funding. Conversely, countries with lack of access to funding (as well as those that never requested it) had to adjust government expenditure and current account balances more than countries with access to IMF financing. Reserve drawdowns were also larger in countries with no access to Fund financing, notwithstanding their stronger current account outcomes.

Evidence from econometric analysis. The mitigating role of Fund financing is confirmed by an econometric analysis of the determinants of post-COVID output loss in countries—measured as the deviation of a country's real output level from its pre-COVID trend—using a panel of 128 EMDEs (74 EMs and 54 LICs) comprising both recipients and non-recipients of Fund financing over the period March 2020 to end-2020. The evidence suggests that Fund financing mitigated losses in recipient countries even after controlling for a long list of other factors that may have influenced output loss during the pandemic.[27] Emergency financing is estimated to have reduced economic losses relative to a scenario of no financing. And when EF was followed by UCT arrangements (or UCT arrangement

FIGURE 28. GDP GROWTH BY ACCESS TO IMF FINANCING, 2020



Source: Batini and Li (2023).

[27] The list of other factors includes: the stringency of NPIs; oil exporter status; measures of countries' fiscal space and fiscal stimulus; international reserves adequacy and reserve drawdowns; the degree of trade openness; and a measure of exchange rate rigidity.

pre-dated EF), the reduction in the economic downturn is estimated to have been even larger; surprisingly, however, financing based on UCT programs alone did not result in statistically significant reduction in losses. Like any econometric analysis, these results need to be interpreted with caution given omitted variable bias (though the long list of controls already included should mitigate this concern) and endogeneity bias arising from correlations between, for example, Fund financing and other variables (though we use a specific lag structure to alleviate this bias).

D. ASSESSMENT

Broadly positive view. Establishing cause and effect is a difficult exercise in any setting in economics and demonstrating an impact from Fund financing on eventual outcomes is no exception. Many developments can transpire between the time that the Fund's financing decisions are made and the time of the measurement of outcomes and many factors other than Fund financing can influence outcomes. Moreover, econometric results can be sensitive to the methodological approach, the data used, and modeling choices. Keeping all these caveats in mind, the evidence presented here nevertheless provides a broadly positive view of the impact of Fund financing: it fulfilled its expected role in helping countries meet their BOP financing needs, it helped relax external constraints by catalyzing support from other sources, and it mitigated output losses arising from the shock. The impact is particularly clear when comparing countries that received Fund financing with those that requested financing but did not receive it.

Fund's role in assisting members to solve their BOP problems. The evidence suggests that Fund financing ended up playing, at least on average, its envisaged role in help addressing BOP financing needs. For EMs, and for LICs receiving EF, the Fund provided the expected 10–15 percent of the financing gap; for LICs receiving UCT financing or both emergency and UCT financing, the Fund's share ended up larger, 25–35 percent on average. As noted in Section III, there is still a question about whether the overall scale of Fund financing was commensurate with the needs of member countries during the pandemic, particularly for countries with exceptionally large needs. Some countries, like small developing states, had a smaller share of needs met from the Fund and thus made larger recourse to their international reserves. Hence, one could still argue that in particular cases, stronger Fund support would have helped countries moderate the adjustment they ended up making through reserve drawdowns or macroeconomic policy choices, although an assessment would need to take account of the risks involved and the role played by partner agencies.

Marshalling support from other official sources. Interviews with staff at evaluation offices at other multilateral institutions suggest that the Fund's financing was perceived as providing a very helpful signal to others in the official sector. This is consistent with the substantially higher commitments made by MDBs in the presence of Fund support than otherwise, particularly in the case of the World Bank. The increased provision of assessment letters was also appreciated, particularly for countries not receiving financing from the Fund, including many in Asia. Evidence from our country cases suggests that in virtually every case, authorities felt that Fund support had a catalytic effect on funding from other multilateral agencies. Hence, the concern expressed by some that there was competition among agencies to provide financing rather than cooperation, which did surface in some of our interviews, does not receive much support.

Challenges in Bank-Fund collaboration. Interviews and staff survey responses do suggest, however, some tensions in the approaches to country financing decisions between the Bank and the IMF. Fund staff felt there was a greater concern with debt sustainability issues and ensuring appropriate medium-run policy settings at the Bank than prevailed at the Fund. At least in part, such tensions seem to have reflected the early strategic decisions at the Fund to rely on emergency financing for COVID-related support while the Bank mainly relied on policy-related lending. As noted, in a number of cases, such tensions complicated the Fund's financing decisions amid uncertainties about how financing gaps would be filled and contributed to much later disbursements by the Bank than by the Fund. At the same time, there were a number of cases where the Bank but not the Fund provided financial support, which seems to have reflected more flexibility in their financial instruments (especially to provide resources on highly concessional terms for humanitarian purposes) and less stigma involved in using Bank lending, particularly in middle-income countries. The collaboration at the level of country teams nevertheless appears to have worked well according to the evidence from case studies and the staff survey. Last but not least, the Bank and the Fund collaborated well on advocating for and operationalizing official debt relief initiatives, such as the DSSI, under the auspices of the G20.

Catalyzing financing from markets. The empirical evidence on whether Fund financing had a catalytic effect on private sector flows is mixed. But it does appear that EMs that requested but were unable to access Fund resources experienced significantly greater net capital outflows. Moreover, our most careful econometric analysis does find modest evidence that recipients of Fund EF experienced higher net portfolio inflows on average than a control group, with the immediate effect stronger for EMs than LICs. Country case studies also suggest that the authorities in most cases felt that Fund financing helped calm financial conditions and assisted in their return to market financing.

Mitigating the COVID-19 shock. Bearing in mind again the caveats associated with establishing causality, our econometric evidence supports the view that emergency financing played a role in mitigating output losses during the pandemic, especially compared to countries that requested but did not gain access to IMF loans.