IEO
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BACKGROUND PAPER

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The IMF's Engagement with Middle East and Central Asian Countries During the Pandemic

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The IMF's Engagement with Middle East and Central Asian Countries During the Pandemic*

Prepared by Adnan Mazarei† and Prakash Loungani‡

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The views expressed in this Background Paper are those of the authors and do not necessarily represent those of the IEO, the IMF, or IMF policy. Background Papers report analyses related to the work of the IEO and are published to elicit comments and to further debate.

* We are grateful for comments and editorial suggestions from Chris Towe.

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ABBREVIATIONS

ADB	Asian Development Bank
BOP	Balance of Payment
ECF	Extended Credit Facility
EF	Emergency Financing
EFF	Extended Fund Facility
EU	European Union
DSSI	Debt Service Suspension Initiative
GDP	Gross Domestic Product
IDA	International Development Association
IsDB	Islamic Development Bank
MCD	Middle East and Central Asia Department (IMF)
PLL	Precautionary and Liquidity Line
RCF	Rapid Credit Facility
RFI	Rapid Financing Instrument
SDR	Special Drawing Right
SPR	Strategy, Policy and Review Department (IMF)
SLL	Short-Term Liquidity Line
SME	Small and Medium-Sized Enterprise
UCT	Upper Credit Tranche
UFR	Use of Fund Resources

EXECUTIVE SUMMARY

Coverage. This paper assesses the IMF's engagement with countries in the Middle East and Central Asian Department (MCD) from February 2020 to April 2021, drawing on the experience of Kyrgyz Republic, Morocco, Tunisia, and Uzbekistan. The paper also briefly describes MCD's policy advice over the course of the pandemic and the department's strategy for helping the region.

Appropriate pivot in surveillance. While staff's initial worries about the region were centered around the sharp spike in global risk aversion—portfolio flows to the region declined by nearly $2 billion in February–March—they quickly pivoted to healthcare and humanitarian considerations. The April 2020 Regional Economic Outlook (REO) emphasized the immediate priority of containing the spread of the virus and advocated fiscal easing to accommodate necessary spending.

Rapid and effective financing. By June 2020, 15 countries in the region had received emergency or upper credit tranche (UCT) financing from the Fund, and the Fund's financing exposure to the region increased by more than 65 percent in 2020. Our case studies of Kyrgyz Republic, Tunisia, and Uzbekistan paint a positive picture overall of the value to countries of the rapid provision of Fund emergency financing (EF). The first two received the maximum permitted under Fund access limits despite some concerns about policies.

- *Kyrgyz Republic:* The speed of support and absence of conditionality were very much appreciated by the authorities and helped improve their uneasy relationship with the Fund. Although the financial support was limited relative to the scale of the shock, the authorities decided not to seek a successor UCT program to the EF.

- *Tunisia:* Fund support was useful in providing resources to Tunisia amid domestic political stresses, global economic uncertainty, and donor hesitancy. Reaching the judgment that Tunisia's debt was sustainable required some "forbearance" on the part of staff. Agreement on a new Extended Fund Facility (EFF) was reached in October 2022.

- *Uzbekistan:* There is a question whether IMF financial support was necessary, given sizable official reserves and policy space. However, the Fund's decision could be justified by the uncertainty about the pandemic's economic impact, the potential catalytic effect of Fund financing, as well as the small risks to the Fund's balance sheet due to the country's strong capacity to repay.

Successful Precautionary and Liquidity Line (PLL) for Morocco. The PLL worked as intended by helping a country with a solid policy framework and track record weather a large external shock through ready, rapid access to Fund resources without conditionality or protracted discussions on policies. The PLL also helped Morocco regain capital market access. The authorities view their experience with the PLL as positive, but noted that they repaid the Fund early to avoid incurring a surcharge.

Difficult cases. Iran's March 2020 request for emergency assistance of US$5 billion has not yet received a definitive response, with the authorities attributing the delay to political considerations.

Governance safeguards. The March Letter of Intent (LOI) for the Kyrgyz Republic—the first country to access Fund EF during the pandemic—and Tunisia's Rapid Financing Instrument (RFI) included limited commitments. Governance safeguards were strengthened over time but monitoring of implementation will remain a challenge.

I. Introduction

1. **Purpose.** This paper assesses the IMF's engagement with countries in the Middle East and Central Asian Department (MCD) during the pandemic, drawing on the experience of four countries that received IMF financing: Kyrgyz Republic, Morocco, Tunisia, and Uzbekistan. Three of these countries received emergency financing (EF)—with the Kyrgyz Republic the first country to receive EF during the pandemic and Tunisia the first to benefit from the doubling of access levels—and the other (Morocco) drew under a precautionary facility. The focus of the assessment is on the period from February 2020 to April 2021. The paper also briefly describes the Fund's overall engagement with the region, including MCD's policy advice over the course of the pandemic and the department's strategy for helping the region.

2. **Sources.** For the four country cases, the narrative provided in this paper is based on interviews with the IMF mission chiefs during 2020–21, several country team members (including resident representatives), senior reviewers within MCD and in the Strategy, Policy and Review (SPR) Department, and the country authorities. Internal documents provided by MCD for the country cases were also consulted. In addition, we interviewed MCD senior staff who were involved in crafting the department's strategy and financing decisions; staff who put together MCD's *Regional Economic Outlook* (REO) reports; Executive Directors and their advisors; and outside experts.

3. **Structure.** Section II summarizes developments in the region during the pandemic and MCD's response to help countries through policy advice and financing.[1] Sections III to VI present the case studies, including our assessment of IMF performance in each case. Section VII concludes.

II. IMF's Engagement with the Region

A. Developments and Policy Advice

4. **Pre-pandemic economic situation.** Prior to the pandemic, the region was already suffering from macroeconomic strains, with subdued growth, vulnerability to a projected slowdown in global growth, and subject to the impacts of geopolitical tensions, social unrest, and regional conflicts (October 2019 REO). Besides the importance of addressing public debt and deficits (especially in the Middle East and North Africa region), the REO highlighted a need to improve longer-term growth prospects through structural reforms. Among the energy exporters, particular emphasis was laid on diversifying the economic base and facilitating private sector-led growth.

[1] The Fund's capacity development and technical assistance work during the pandemic are covered in a separate IEO evaluation (IEO, 2022) and summarized in a background paper for this evaluation (Batini and Wojnilower, 2023).

5. **Onset of the pandemic.** By February 2020, as work was underway on the April 2020 REO, these longer-run considerations had to be balanced against the immediate need to counter the likely effects of the pandemic on the region. Staff's initial worries were centered around the sharp spike in global risk aversion—portfolio flows to the region declined by nearly $2 billion in February–March—and tightening financial conditions, seen as particularly challenging given $35 billion in maturing sovereign debt in 2020. However, as concerns about the possible health consequences from the pandemic became more prominent in the region, influenced particularly by the experience of Iran, which was facing a severe outbreak, the policy imperative pivoted to healthcare and humanitarian considerations.

6. **Fund advice.** Staff recognized that the region's resilience in the face of the pandemic was handicapped by low levels of health expenditures and infrastructure in many countries. And fragile states in the region were additionally vulnerable in light of their large refugee populations, heavy reliance on informal economies, and limited fiscal resources. The April 2020 REO (IMF, 2020e) therefore emphasized the immediate priority of containing the spread of the virus and advocated fiscal easing to accommodate necessary spending, a message reiterated by the MCD Director in his interactions with officials and in press interactions: "The immediate priority is to save lives. Governments should continue to accommodate essential health spending, delaying non-essential spending to create space if needed" (Azour, April 15, 2020). Staff also advocated allowing exchange rates to depreciate to absorb the demand-side shock, but also acknowledged that tighter monetary policies might be needed where there was a risk of disruptive capital outflows. In addition, the REO advised that consideration could be given to a temporary easing of prudential and regulatory measures, such as adjusting loan-to-deposit ratios and deferred loan payments.

7. **Policy response by governments.** The initial fiscal policy response in the MCD region was significant but generally on a smaller scale than in other regions, reflecting the limited policy space available among oil importers and already sizable government support for the economy among oil exporters. And in many cases, these fiscal spending packages were offset by expenditure reallocations or revenue measures. As financial conditions stabilized with strong actions by advanced economy central banks, most countries in the region were also able to cut policy interest rates sharply in March–April 2020 and roughly half the countries in the region provided substantial liquidity to their financial systems. In countries with flexible currencies, exchange rates were allowed to depreciate, and roughly half the countries in the region also eased macroprudential policies. The need for capital flow management measures turned out to be limited and they were scarcely used.

8. **Mid-2020 forecasts and advice.** These policy measures notwithstanding, the economic impact of the pandemic was severe as a result of the lockdowns and other policies designed to stem the spread of infections, a cut in remittance inflows, and spillovers from the disruption to global value chains and slowdowns in key trading partners. Oil exporters were further affected by the sharp decline in oil demand and prices. The IMF's mid-2020 WEO forecast for the region was

for a decline of 4.7 percent in 2020.[2] The July 2020 REO's policy advice maintained its call for macroeconomic support and warned against "unwinding emergency measures in a disruptive way."

9. **2020 outcomes.** The pandemic had significant humanitarian and health consequences on the region as infection rates surged through mid-2020. However, despite another surge starting in the fall of 2020, economic outcomes for the year turned out to be less severe than forecast. According to MCD staff responsible for the forecasts, there was "varying degrees of top-down guidance, heaviest early on in the crisis" from the Research Department (RES) WEO group but there was such uncertainty in the early months that "this was probably the only way to go." In hindsight, where top-down guidance may have gone somewhat astray, according to MCD staff, was in leading some country desks to assume that the GDP impacts of mobility restrictions in US and EU could be used to project the impact of restrictions elsewhere. But in many MCD countries with high degrees of informality, countries were either not willing to impose similar lockdowns as in advanced economies or the lockdowns' impact on activity ended up being smaller than in advanced economies.

10. **Calibration of policies and Fund policy advice.** With 2020 outturns turning out better than expected in some countries, policy advice in the October 2020 REO started to turn to considering an eventual exit from macroeconomic support. During 2021, despite surges in infection rates, infection and death rates remained relatively contained, especially among those countries that had made early progress in vaccinations. With the easing of the COVID-19 infection and death rates, regional GDP rebounded by nearly 6 percent in 2021, driven by a recovery of domestic demand, a rebound in remittance inflows, and a revival of non-oil GDP among oil exporters. The recovery in economic activity, and growing concerns about inflation and debt sustainability, led to policy supports being gradually withdrawn in 2021. Countries with flexible exchange rates began to raise interest rates, although rates in real terms still remained below pre-pandemic levels, and most macroprudential policy measures were allowed to expire.[3] Staff supported the thrust of these policies in the REO, but advised continued recognition that the pace of consolidation would need to be calibrated not just to economic considerations such as available fiscal space and the credibility of monetary policy, but to health considerations as reflected in rates of infection and access to vaccines. Staff also took note of the sluggish recovery in employment and devoted an analytic chapter to analyzing and offering advice on how to mitigate longer-term scarring effects on the labor market.

[2] Officials in some countries were initially reluctant to project recessions ("they hadn't seen this before") but soon realized that everyone was going to be in negative territory.

[3] However, emergency fiscal spending measures were extended in a number of countries that experienced a resurgence of the pandemic.

B. Strategy and Financing Decisions

11. **The Fund's overall strategy.** As described in the background paper by Ocampo and others (2023), during February 2020 the Fund worked toward a strategy for financial support to countries emphasizing: (i) recourse to EF—the Rapid Financing Instrument (RFI) and the Rapid Credit Facility (RCF)—instead of new upper credit tranche (UCT) arrangements or a new facility; (ii) urging use of existing precautionary facilities and launch of a new short-term liquidity line (SLL); (iii) use of the Catastrophe Containment and Relief Trust (CCRT); (iv) push for a SDR allocation; and (v) help to countries through debt relief and consideration of debt treatments where needed. MCD senior staff were comfortable with the reliance on existing EF, which they considered to offer enough flexibility to meet the immediate needs of their countries, and "lukewarm" to the idea of a new facility. They were skeptical about take-up of the SLL as MCD countries would not likely meet the qualifying criteria and initial discussions with some authorities suggested they found the terms and conditions too onerous. Like other area departments, MCD would have preferred to offer countries more EF at the outset but they recognized that the Board may be "uncomfortable about giving out too much money unconditionally" and it may be better to proceed in gradual steps.

12. **Implementing the strategy to meet regional needs.** Within the parameters of the Fund's overall strategy, MCD staff had to consider how to support the 32 countries in their region, which are divided about equally between high-income, middle-income and low-income countries (LICs), and also differ in other ways, a notable distinction being between the oil exporters and the oil importers. A sizable number are fragile and conflict-afflicted states. Interviews with MCD senior staff reveal that their initial thinking was to cluster countries into three groups: a group that could be provided rapid access to EF; a second group of countries that would not need emergency financial support; and a third group where providing financial support would be challenging and support would have to be provided through other means such as technical assistance. MCD's expectations were that despite oscillations in oil prices, oil exporters in the region had financial resources to tide them over and would not need Fund financing. A few countries had sufficient access to other official borrowing. Together, this made up a group of 12 countries.[4] There were five cases where staff felt that financial support would be "difficult" for various reasons—these were Iran, Lebanon, Libya, Sudan, and Syria. Overall, during 2020–21, 17 countries had received emergency or UCT financing from the Fund, as well as debt relief under the CCRT (Table 1).

[4] The 12 countries are Algeria, Azerbaijan, Bahrain, Iraq, Kazakhstan, Kuwait, Oman, Qatar, Saudi Arabia, Turkmenistan, UAE, and West Bank and Gaza. All are oil exporters except the last in the list; West Bank and Gaza, along with Azerbaijan and Turkmenistan, had access to other official borrowing. In principle, Uzbekistan—an oil producer—could also have been on this list, as discussed in Section VI.

Table 1. IMF Financing, 2020–21

Member	Instrument Type	Amount of Emergency Financing/Debt Relief Received		
		Millions of US$	Percent of GDP	Percent of Quota
Afghanistan	ECF	370.0	1.9	80.0
	CCRT	10.0	0.1	n.a.
	RCF	220.0	1.2	50.0
Armenia	SBA	175.0	1.3	100.0
Djibouti	CCRT	7.5	0.2	n.a.
	RCF	43.4	1.3	100.0
Egypt	RFI	2772.0	0.9	100.0
	SBA	5200.0	1.7	184.8
Georgia	EFF	375.6	2.2	130.0
Jordan	EFF	1505.5	3.3	312.0
	RFI	396.0	0.9	85.0
Kyrgyz Republic	CCRT	12.5	0.1	n.a.
	RCF	80.7	0.9	33.3
	RFI	161.3	1.8	66.7
Mauritania	ECF	28.7	0.4	15.7
	RCF	130.0	1.7	74.3
Morocco	PLL	2970.0	2.5	240.5
Pakistan	RFI	1386.0	0.5	50.0
Somalia	ECF	131.9	2.7	59.7
	EFF	263.7	5.3	119.3
Sudan	ECF	2472.7	7.1	275.0
Tajikistan	CCRT	25.5	0.3	n.a.
	RCF	189.5	2.4	80.0
Tunisia	RFI	745.0	1.9	100.0
Uzbekistan	RCF	125.0	0.2	16.7
	RFI	249.3	0.4	33.3
Yemen	CCRT	59.4	0.3	n.a.

Source: IMF.

13. **"Difficult" cases:** Iran was one of the first countries in the region to be severely impacted by the pandemic and was singled out as such in the April 2020 REO, and by this time the authorities had requested financing under the RFI. In June 2020, the Board was assured during an informal briefing of "continuing engagement with the Iranian authorities" and management noted that "Iran's request would come to the Board once due diligence has been completed." In October 2020, responding to concerns at the Board during an informal MCD regional briefing about lack of evenhanded treatment of Iran, staff stated that Iran was a "complex case which required additional work," particularly with regard to the establishment of a balance of payments (BOP) need and with regard to safeguards. Iran's request remains open according to staff (see Box 1). Among the other challenging cases was Lebanon, where the authorities approached the Fund for financing, but with the government falling in August 2020 staff felt there was no counterparty to make commitments to the policies needed to provide assurance of repayment to the Fund.

Box 1. Iran

Iran has been one of the countries most affected by the health consequences of the pandemic. The authorities requested in March 2020 US$5 billion in emergency assistance under the RFI to help address the health and economic impact of the pandemic. Thus far, Iran has not yet received a definitive response from the Fund. The Iranian authorities have repeatedly criticized the Fund for discriminating against Iran for political considerations.

While Iran is a middle-income oil producer, its international economic transactions, including oil exports and banking relations, have been sharply curtailed by U.S. primary and secondary sanctions. It has lost access to most of its sizable official reserves. The effects of the sanctions, and problems in economic management, have led to a sharp drop in economic activity, high inflation, and significant problems in the banking sector. Financial transactions were also hampered by Iran being put by the Financial Action Task Force (FATF) on its blacklist. The authorities have stated that Iran's access to medical equipment needed to fight the pandemic has been curtailed by these restrictions.

Since its request, staff have engaged with the Iranian authorities on conditions needed to support access to the RFI. However, factors hampering Iran's request included:

- Issues related to the provision of data by Iran on the state on the Iranian economy, including about the portion of Iran's official reserves that was accessible by the authorities.
- The difficulty of finding channels that could be used for Iran to receive Fund financing in the face of U.S. sanctions. Likely candidates have been two vehicles established in Europe to facilitate humanitarian trade: (i) INSTEX, a facility set up by France, Germany, and the United Kingdom, and (ii) the Swiss Humanitarian Trade Arrangement. However, these channels would have been difficult to use for the large sum of US$5 billion requested by Iran.

14. **EF or UCT?** At the start of the pandemic, some countries (Armenia, Georgia, Mauritania, Pakistan, and Tunisia) were in UCT programs, and a decision had to be made on whether continuing with the program or switching to EF would be the faster mode for providing support during the pandemic. In the end both methods were used. In particular, Armenia benefited from an augmentation and re-phasing of its program, and a similar path was followed in the case of Georgia. For Tunisia, the Extended Fund Facility (EFF) was canceled and EF was used.

15. **Governance safeguards.** In interviews, MCD staff noted that while the Board appropriately wanted assurance that money was being "used for the right purposes," implementation of the safeguards posed difficulties because procurement practices in the region were "not of the same standard" as elsewhere and the beneficial ownership framework was generally not in place. MCD staff felt that Fund treatment on governance safeguards could have been more "forward-looking," requiring commitments to future reforms in transparency, rather than requiring prior actions in the form of immediate changes which were difficult to implement.

16. **Relationship with partner agencies.** Staff noted that the MCD Director had regular interactions with his counterpart at the World Bank, the Regional Vice President for the region, prior to the pandemic. These interactions continued through the pandemic and set a good tone for collaboration between the institutions. Interviews with IMF staff, as well as with World Bank staff interviewed as part of the IEG's parallel evaluation, confirm frequent and productive interactions between Bank-Fund country teams. As noted in the case studies that follow, MCD

also coordinated with other donors, such as the Asian Development Bank (ADB), the Islamic Development Bank (IsDB) and other partners, including in the context of the Debt Service Suspension Initiative (DSSI).

III. KYRGYZ REPUBLIC

Kyrgyz Republic was the first country to receive emergency assistance from the IMF, through the RFI and RCF. There were two packages: in March 2020 (50 percent of quota, or US$121 million), and May 2020 (another 50 percent, US$121 million) after Fund-wide access limits were doubled. There have been no discussions toward a follow-on UCT program.

A. Background and Economic Developments

17. **Initial conditions.** Prior to the pandemic, economic growth was steady, but too low to raise living standards and make a dent in the very high poverty level. While inflation was low, the economy was vulnerable on account of its dependence on remittances and gold exports, the level and composition of its public debt (52 percent of GDP, mostly denominated in foreign currency), and large current account deficit of 12 percent of GDP (Table 2). Eight successive Fund arrangements had supported programs aimed at strengthening public finances, including through gradual reductions in tax exemptions, energy subsidies, and the wage bill. To raise growth rates and incomes, programs had included measures which sought to address corruption and build respect for the rule of law, improve the business climate, and improve infrastructure and financial sector development. However, the programs had limited traction and the last Extended Credit Facility (ECF) expired in April 2018, owing to differences of views between staff and the authorities on policies.

Table 2. Kyrgyz Republic: Selected Economic Indicators

	2019	2020					2021		
	Actual[1]	Projections Pre-COVID[2]	Projections March[3]	Projections May[4]	June WEO	Actual[1]	Projection Pre-COVID	June WEO	Actual[5]
GDP growth (Percent)	4.6	3.4	0.4	-4.0	-12.0	-8.6	3.8	9.8	3.7
Inflation (Percent)	1.1	4.9	10.6	10.6	8.8	6.3	5.0	2.7	11.9
Budget balance (Percent of GDP)	-0.1	-3.0	-7.8	-8.8	-7.5	-3.3	-3.0	-5.7	-1.3
Government debt (Percent of GDP)	51.6	55.5	65.9	69.0	65.4	68.0	55.5	61.1	61.0
Current account balance (Percent of GDP)	-12.1	-7.7	-14.5	-13.1	-13.1	4.5	-7.6	-13.0	-5.2
External public debt (Percent of GDP)	43.3	46.7	56.5	59.1	56.1	58.3	45.8	52.7	52.3
Official reserves (USD Billions)	2.2	1.9	1.9	1.9	2.1	2.6	1.9	2.0	2.6

[1] Staff Report for 2021 Article IV Consultation (Country Report 21/174).
[2] Staff Report for the 2019 Article IV Consultation (Country Report 19/208).
[3] Staff Report for First RFI/RCF Request (Country Report 20/90).
[4] Staff Report for Second RFI/RCF Request (Country Report 20/158).
[5] IMF WEO 2021.

18. **Impact of the pandemic and policy response.** The pandemic hit the economy hard. The border with China, a major trading partner, was closed, which hurt economic activity and collection of border taxes. Tourism and remittances, especially from Russia where oil prices had declined, fell significantly; transportation, trade, and construction suffered. In the early months of the crisis, the currency depreciated sharply, contributing to a surge in consumer prices.

19. **Policy response.** The fiscal stance was relaxed significantly in the early months of the pandemic; the deficit was expected to rise, though with most of the increase coming from a revenue shortfall (Table 2). Health spending in the original budget was to be protected, but with only a small amount in additional measures for fighting the pandemic and its economic impact, which included tax postponements, and temporary exemptions on property and land taxes. Subsequently there was a much larger package that included temporary tax relief and loans for small and medium-sized enterprises (SMEs), and food support for the vulnerable.[5] The central bank raised interest rates and intervened to support the currency. It also showed flexibility on the timing of rebuilding banks' capital and liquidity adequacy requirements. Despite the policy response, there were public protests of the economic difficulties related to the pandemic and to the change in government in early-October 2020.

B. Engagement with the IMF

20. **March 2020 EF drawing.** On March 26, 2020, the Kyrgyz Republic was the first member country to gain approval of emergency IMF assistance to combat the pandemic. While the Kyrgyz Republic had long-standing challenges that would have normally required a UCT program, staff suggested EF on account of the difficult circumstances and the complexities that negotiating a UCT program would have entailed. Despite the initial uncertainties in the Fund about the institution's modalities for assisting pandemic-affected countries, staff was able to reach agreement on a letter of intent and economic framework with authorities in three weeks, aided by having a resident representative for the country. The framework envisaged a significant economic deterioration from the pandemic (Table 2). Growth was projected to decline to 0.4 percent in 2020, compared with 4.6 percent the year before. The budget deficit in 2020 was anticipated to deteriorate to 7.8 percent of GDP from near balance the year before, mainly due to lower revenues, and the current account was expected to deteriorate sharply to 14.5 of GDP, contributing to an external financing gap of about US$400 million.

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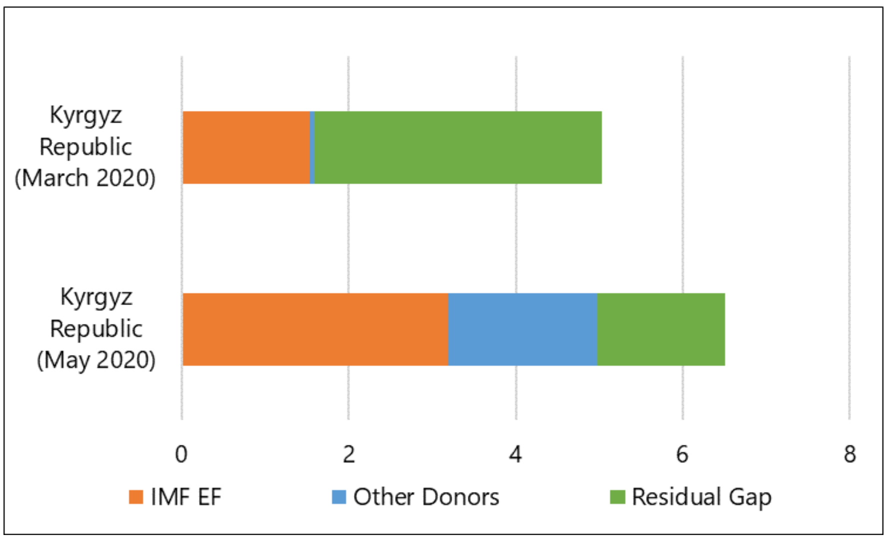
[5] Compared to 2019, in 2020 government spending rose on social contributions (0.3 percent of GDP), compensation of employees (1.8 percent of GDP), and social benefits (0.9 percent of GDP)—see IMF Country Report No. 21/174. These amounts may not include all the pandemic-related spending by the government. Nor are these figures necessarily comparable with COVID-related spending information reported for the other three other case studies reported in this paper.

21. **RFI/RCF blend.** The Fund provided financial assistance through a blend of RFI and RCF resources because Kyrgyz Republic's gross national income per capita exceeded the International Development Association (IDA) threshold.[6] The Fund provided a total of about US$120 million (50 percent of quota—the maximum access level allowed then under emergency assistance), combining concessional financing under the RFI (US$80 million, 33 percent of quota) and the RCF (US$40 million, 17 percent of quota). Despite the assistance committed by the Fund and other donors and expected reserve drawdowns, the program had a residual financing gap of nearly 2 percent of GDP (Figure 1). These financing needs could not be met by the Fund because of the emergency financing (EF) access limit of 50 percent of quota, but discussions with other donors had indicated that Fund support would likely catalyze additional resources. Staff thought that debt distress risks were moderate, and that debt would remain sustainable even if the shock from the pandemic was larger than assumed under the program.[7] Staff also thought that the banking system would be resilient to a short-lived crisis.

Figure 1. Kyrgyz Republic: Ex Ante Balance of Payments Gap, 2020
(In percent of GDP)



Sources: Staff Report; IEO staff calculations.
Note: Following Kincaid, Cohen-Setton and Li (2022), reserve drawdown is treated as financing.

22. **May 2020 EF drawing.** With the IMF raising its EF access limit to 100 percent of quota and considering the Kyrgyz Republic's worsened economic outlook, in May the Fund provided additional support of US$120 million with the same financing mix as the March program. The total resources made available by the Fund to the country were thus about US$245 million—the new maximum access limit of 100 percent of quota. Under the revised framework, taking into

[6] The authorities were disappointed that the financing package carried an interest rate that exceeded zero, in part because this created procedural difficulties for them with respect to Kyrgyz Republic's external borrowing procedures.

[7] Kyrgyz Republic was eligible for DSSI relief. It received relief in September 2021, for debt service due during July–December 2021. The delay in agreement related to reaching understandings with China.

account the expected support from the ADB and the World Bank, there was still a residual but smaller financing gap (Figure 1). By the time of the May package, staff's analysis of the outlook for 2020 was changed in some respects compared with the March program. The economic contraction was expected to be much worse, the budget deficit larger, and the current account deficit a bit smaller (see Table 2).

23. **Economic outcomes.** The economy contracted 8.6 percent in 2020, a sharp decline but less than expected mid-year, and rebounded in 2021, growing by 3.7 percent. Inflation picked up to 11.9 percent, due to higher food and fuel prices. The budget deficit declined to 1.3 percent of GDP on account of improved revenue administration and expenditure restraint, contributing to a decline in public debt.

C. Assessment

24. **Overall assessment.** The staff's strategy was to provide room for the Kyrgyz government's fiscal response to the pandemic by supporting a temporary loosening of policies, quickly providing financing, and catalyzing support from other donors. The support from the IMF helped Kyrgyz Republic allay the economic consequences of the pandemic, although it is hard to assess the impact and adequacy of Fund assistance on health services and the social safety nets. It was difficult for Fund staff to assess the needed spending in these areas in the midst of a pandemic. The use of the RFI/RCF as instruments of Fund support was appropriate. The speed of support and absence of conditionality were very much appreciated by the authorities and helped improve the sometimes-uneasy relationship with the authorities. The total amount of IMF support was small relative to the scale of the shock, but the authorities were not inclined to pursue a UCT program that would have been needed to justify higher use of Fund resources (UFR).

25. **Staff analysis and projections.** The 2020 outcomes were quite different than expected:

- The economy contracted by 8.6 percent, considerably more than the 0.4 percent and -4.0 percent, respectively, expected under the March and May economic frameworks, The anti-pandemic measures, including border closures, had a larger-than-expected impact on trade and investment, and political turmoil in October also took a toll on growth. The outcome was, however, not as dire as expected in the June 2020 WEO.

- The fiscal deficit was much smaller than envisaged. There were cutbacks in capital outlays and spending on services, due partly to shortfalls in domestic revenues from the larger-than-expected economic contraction, and partly to falls in donor financing following public protests attributed to the economic difficulties related to the pandemic and to the change in government in early October 2020.

- The current account ended with a surplus, instead of the deficits envisaged. This was partly related to a recovery in remittances and a sharper-than-envisaged import compression as the border closure with China was more severe than expected. But the official figures may overstate the current account position.[8] The surplus contributed to an accumulation of reserves in 2020, instead of the envisaged drawdown, notwithstanding lower donor support.

26. **Access.** In interviews, the authorities indicated that access was adequate, though they felt that the Kyrgyz Republic merited more concessional terms. That said, however, total access may have been insufficient viewed through the lens of the country's needs. First, in the March and May frameworks, access was constrained by the Fund's limits, and there were sizable unidentified budget financing gaps. The more-difficult-than-envisaged economic outturn in 2020 also suggests that the Fund could have provided more assistance, especially after some donors curtailed their support on account of the protests and change in government in October 2020. However, given the deep-seated problems in the Kyrgyz economy and the authorities' mixed record of policy implementation, an increase in Fund financing may not have been prudent without a UCT program.[9] This was in part because, as noted by staff in interviews, there was not an adequate focus on debt issues during program formulation. In retrospect, therefore, the lack of progress on reforms and a successor program justifies the prudence shown by the Fund regarding access.

27. **Policies.** The staff have for long thought that fundamental policy reforms were required to address Kyrgyz Republic's economic troubles. Arguably Kyrgyz Republic needed a UCT program. Nevertheless, given the Fund's overall approach of providing financial support without major policy reforms to address the immediate health challenges in the initial emergency phase of the pandemic, the staff responded expeditiously, without agreement on a package of deeper policy adjustments. This was pragmatic use of the flexibility under the EF, given the lack of clarity about the course of the pandemic and its channels of economic impact, especially in economies with sizable informal sectors. In view of the measures needed to fight the pandemic, fiscal policy targets were relaxed. Given the lower-than-envisaged budget outturn for 2020 and the difficulties with poverty and unemployment, a more accommodative fiscal stance than that which eventually materialized could have been warranted. However, such an approach was not feasible given the limits on Fund EF access, the pullback in donor support and the authorities' unwillingness to make commitments needed for a UCT arrangement. The authorities and staff were generally on the same page regarding monetary and exchange rate policies, with the staff stressing that: (i) the central bank should provide liquidity to banks; (ii) exchange rate overshooting should be countered but a depreciation should be accepted if it reflected changes in fundamentals; and (iii) a temporary increase in inflation should be accommodated, but monetary policy tightened if inflation persisted.

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[8] There was a large, negative errors and omissions figure in the balance of payments for 2020, which could be due to unrecorded imports. Including this figure would lower the current account surplus for that year substantially.

[9] The staff report for the March program had already warned that the impact of pandemic could be larger than envisaged, in which case a UCT program would to be needed.

28. **Governance safeguards.** The March LOI included commitments to conduct an ex post audit of the procurement of emergency medical supplies and to publish the results. While Kyrgyz Republic had well known governance issues, the Fund was not requiring deeper steps to provide strong safeguards at this stage. The authorities also agreed to keep IMF financing in a government account at the central bank pending their use. Governance safeguards were strengthened in the May program, under which the authorities committed to publishing bidding documents for competitive and single tender procurement, including those of state-owned enterprises and joint-stock companies with majority state shares and their subsidiaries. The May LOI program also included a commitment to publish procurement documents, verification of delivery, and beneficial owners.[10]

29. **Relations with partners.** Before the pandemic, there was already an effective donor coordination framework in place among the major international institutions. That said, Fund staff felt that, during the pandemic, other donors were in general waiting for the Fund to lead with financial assistance, and more simultaneity in provision of support based on joint assessment of needs might have served the country better. The ADB, EU, and the World Bank did follow the Fund's lead in committing financial support during the pandemic, but also pulled back in the face of uncertainties created by public protests and the political transition late in the year.

IV. MOROCCO

Morocco was the only country that received financing under the Precautionary and Liquidity Line (PLL), approved in December 2018.[11] This purchase for US$3 billon (240 percent of quota) was made automatically on request, per PLL procedures, and the Executive Board was informed ex post.

A. Background and Economic Developments

30. **Initial conditions.** Prior to the pandemic, Morocco's economic fundamentals and policy framework were generally sound and had been supported by several PLL arrangements starting in 2012. Gains were made with economic diversification and participation in global value chains, the banking system was generally sound, and there was steady access to international capital markets at relatively low spreads. Fund staff advice centered on the need for structural reforms in governance and combatting corruption, access to finance, and the labor market to strengthen private-sector growth. Public debt was seen to be sustainable, but high enough to pose risks. The external position was also seen as sustainable, yet the staff counselled that there was a need to make the exchange rate system more flexible to make the balance of payments more resilient.[12]

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[10] In interviews, staff said that the Kyrgyz Republic did not have regulations regarding beneficial owners, and changes to laws were made to introduce such regulations.

[11] The only other country with a PLL during the period under examination by this IEO review was Portugal. The arrangement was agreed in January 2021. The authorities have treated it as precautionary and not made any purchases.

[12] See the staff report for the second review under Morocco's PLL.

There was also a need to strengthen social spending and the safety net, including to address the discontent that had surfaced during the Arab Spring. In 2019, growth was weak, at 2.5 percent (Table 3), insufficient to lower the high unemployment rate, especially among women and the youth. Inflation was low. Fiscal space was constrained by a budget deficit of 4.1 percent of GDP and a government debt of 65 percent of GDP; the current account deficit was 4.1 percent of GDP, but international reserves were comfortable (Table 3). IMF staff warned about macroeconomic risks, especially those related external factors including Euro area growth, geopolitics, and global financial conditions.

Table 3. Morocco: Selected Economic Indicators

	2019	2020					2021		
	Actual[1]	Projections Pre-COVID[1]	Projection COVID[2]	Projection COVID[1]	June WEO	Actual[3]	Projection Pre-COVID	June WEO	Actual[3]
GDP growth (Percent)	2.5	3.7	-3.7	-7.2	-7.4	-6.3	4.1	4.9	7.2
Inflation (Percent)	0.2	1.2	0.3	0.2	0.2	0.6	2.0	1.2	1.4
Budget balance (Percent of GDP)	-4.1	-3.8	-7.1	-7.7	-8.3	-7.6	-3.0	-5.5	-6.5
Government debt (Percent of GDP)	65.0	65.7	73.7	76.5	77.6	75.4	63.2	77.2	76.3
Current account balance (Percent of GDP)	-4.1	-3.9	-7.8	-6.0	-7.0	-1.5	-3.1	-4.4	-2.9
External debt (Percent of GDP)	32.8	32.7	38.1	39.7	36.5	41.7	30.8	35.9	40.5
Official reserves (USD billions)	26.4	25.8	23.2	32.0	24.0	35.3	27.8	26.4	35.6

[1] 2020 Article IV Report (IMF Country Report No. 21/2).
[2] FO/DIS/20/69.
[3] IMF WEO 2021.

31. **Impact of the pandemic.** The pandemic and the authorities' containment measures hit the economy hard. The government declared a state of heath emergency and put in place confinement measures and restrictions on domestic and international travel. Separately, economic activity was hurt by a drought that hit agriculture. There was early success in containing the pandemic up to July 2020, when restrictions were eased, but then a second wave of contagion followed.[13] Staff had initially expected a V-shaped recovery, and both they and the authorities thought that the drawing under the PLL and other financing already secured at the time of the PLL drawing would be adequate to cover the expected substantial deterioration in the BOP without serious pressure on international reserves. In the event, however, the hit to the economy was larger than expected. GDP contracted by 7.4 percent in 2020, the first contraction since 1997 (Table 3), much more than the staff envisaged at the time of the PLL purchase. The unemployment rate picked up from 9.2 to 11.9 percent and poverty rose. There was a decline in exports, tourism, and capital inflows. There was also a drop in manufacturing activity and

[13] See the World Bank's Morocco Economic Monitor: From Relief to Recovery, Fall 2020.

imports, especially those tied to the Euro area, including automobiles, aeronautics, and textiles. The decline in imports, together with some resilience in remittances, helped cushion the impact of the crisis on the current account and overall BOP. The exchange rate weakened in the early months of 2020, yet it appreciated in real effective terms by the end of the year. Equity prices fell sharply in early 2020 but recovered in the remainder of the year.

32. **Fiscal policy response.** The government created an emergency committee to coordinate the response to the pandemic. It set up a COVID Fund of about 3 percent of GDP, to be financed by both public and private contributions, to cover medical expenses, and support households (including those in the informal sector) and businesses.[14] The authorities provided temporary cash transfers to the unemployed, as well as debt service and income tax repayment relief. Firms were supported through a credit program, including the provision of working capital at subsidized rates, and loans provided to the self-employed. These steps raised the budget deficit from 4.1 percent of GDP in 2019 to 7.6 percent in 2020, compared with a 2020 budget deficit of 3.8 percent of GDP envisaged in the PLL. More than 2 percentage points of GDP of the increase in the deficit was on account of cash transfers, and 1 percentage point because of increases in wages and salaries.[15] The authorities did not scale up health spending in 2020, but they tried to remedy this in 2021. The fiscal position was hurt not just by higher spending, but also a loss in tax revenue. Government debt rose from 65 to 75.4 percent of GDP.

33. **Monetary policy.** The central bank eased monetary policy and provided both dirham and foreign currency liquidity to banks, which initially reduced its official reserves. It cut its policy rate, expanded the range of collateral for repos to banks, provided foreign currency swaps, eliminated reserve requirements, and relaxed macroprudential requirements. The central bank also widened the exchange rate fluctuation band from +/- 2.5 percent to +/- 5 percent (staff had advised increased exchange rate flexibility and a move to inflation targeting long before the COVID-19 pandemic). The authorities borrowed from bilateral and multilateral sources beside the IMF and tapped the international bond market. With these measures, the sharper-than-expected compression in imports, and international borrowing, the central bank was able to build official reserves by end-2020. Since inflation remained subdued during 2020, staff was supportive of the central bank's accommodative stance and recommended it be continued unless signs of inflation pressures appeared. The financial system appeared to have coped with the effects of the economic contraction, although nonperforming loans rose.

[14] Compared with 2019, in 2020 government spending was raised on compensation of employees (0.9 percent of GDP) and social benefits (1.8 percent of GDP). Subsidies were lowered (0.2 percent of GDP). See the staff report for the 2021 Article IV Consultation.

[15] Healthcare assistance did not rise in 2020, but it was budgeted to rise by 8.5 percent of GDP in 2021.

B. Engagement with the IMF

34. **Drawing on the PLL.** In response to the pandemic, on April 7, 2020, Morocco drew the full amount available to it under the PLL—about US$3 billion, equal to 240 percent of quota and about 3 percent of GDP.[16] This was consistent with the PLL procedures that allowed an automatic drawing; a PLL drawing has no conditionality attached to it, and Fund resources are expected to be safeguarded by the earlier assessment of the member's policy track record and policy framework at the time of PLL approval. Staff informed the Executive Board and subsequently issued a note explaining the circumstances that had led to the tapping of Fund resources. A press release was issued, but there was no staff report or detailed macro projections—again consistent with PLL procedures.[17]

35. **Determination of access level.** The access level of US$3 billion had been determined at the approval of the PLL in 2018 based on staff's assessment at that time of the risks to Morocco's BOP. With the advent of the pandemic shock, however, staff thought that Morocco could face pressures higher than envisaged at the time of PLL request. Hence, they believed that drawing the full amount (as well as support from other multilateral institutions) was justified to strengthen central bank reserves to a level exceeding the threshold used to determine the PLL access level (80 percent of the Fund's Assessing Reserve Adequacy, ARA, metric) in 2018.

36. **2020 outturn.** The current account deficit for 2020 ended up at only 1.5 percent of GDP vs. the 6.0 percent projected (Table 3), due in good part to the larger-than-expected import compression (mainly imports of energy and of capital goods used in the production of manufacturing goods exports, especially to the Euro area), remittances were also better than expected. The turnaround in market access was also quicker and stronger than most observers, including the staff, had anticipated. Perhaps catalyzed by the PLL, the authorities were able to issue bonds amounting to US$1 billion in September and US$3 billion in December 2020. Official reserves thus ended up much higher than staff expected at the time of the PLL purchase.

C. Assessment

37. **Overall assessment.** The PLL worked as intended by helping a country with a solid policy framework and track record weather a large external shock through ready, rapid access to Fund resources without conditionality or protracted discussions on policies. Although PLL resources were used by the central bank for liquidity support, they indirectly created space for the government to absorb a larger budget deficit. The PLL also helped Morocco regain capital market access. In the event, Morocco was able to rebuild reserves quickly, enabling it to repay

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[16] The PLL was scheduled to expire on December 16, 2020, but with the full purchase, it automatically expired on April 7, 2020.

[17] See the Press Release: https://www.imf.org/en/News/Articles/2020/04/08/pr20138-morocco-draws-funds-available-under-precautionary-liquidity-line-covid19-pandemic.

the Fund early, in January 2021. The economy rebounded sharply in 2021, with GDP growing at 7.2 percent, inflation remaining low, the budget deficit falling slightly, but with the current account deficit rising to 2.9 percent of GDP.

38. The early repayment highlighted one possible shortcoming of the PLL as part of a pandemic response, namely its high cost. The authorities attributed their decision to repay to the fact that they wanted to avoid paying a surcharge, noting that Fund resources were more expensive than market financing at the time of repayment.[18] In interviews, officials expressed concern about the Fund's high surcharge rates, suggesting that their use to support the Fund's income conflicted with the role of the Fund in providing financial support to its membership. In staff's view, Fund's surcharges are designed to provide incentives to limit the size of Fund arrangements and encourage members to make repurchases in a timely manner when they regain market access or when their spreads tighten; hence, they regarded Morocco's early repurchases as evidence that the intended incentives provided by surcharges actually worked.

39. **Access.** In retrospect, the access level, which was determined at PLL approval well before the pandemic, was adequate. The size of the purchase was a key factor that helped rebuild market confidence, thus containing the economic damage from the pandemic. Had the shock been larger than that which materialized, a higher access level may have been needed.

40. **Policies.** The staff and the authorities generally agreed on the actions needed to allay the economic impact of the pandemic, aided by a prior history of generally effective policy discussions. In discussions in April 2020, staff concurred with the authorities on the need for an expansionary fiscal stance and allowing the deficit to increase much more than envisaged. In interviews, staff suggested that they would have liked to see more health spending; the authorities, however, believed that the increase in such spending was adequate. They welcomed the widening of the exchange rate band and flexibility, a policy they had long advocated. Later in the year, the 2020 Article IV discussions (IMF Country Report No. 21/2) paid particular attention to the need for gradual fiscal consolidation, including containing fuel subsidies, but only after recovery was firmly under way,

41. **Staff projections.** The growth impact of the crisis was more severe than the staff anticipated in April 2020 at time of PLL drawing. However, these judgements were complicated by the novelty of the shock and the uncertainty about its size and spillovers, especially with regard to the impact of the drop in demand from the Euro area and its effects on Morocco's imports for capital goods and other inputs for exports. The latter effect exacerbated the growth decline but also resulted in the current account deficit being much smaller than that projected in April due to import compression.

[18] In addition, by lowering the amounts outstanding to the Fund to below the 200 of quota threshold, Morocco avoided the Post-Program Monitoring that would otherwise have been required.

42. **Governance safeguards and safeguards assessment.** The PLL, which was agreed well before the pandemic, did not incorporate any governance-related measures to ensure the proper use of COVID-related spending. However, the General Inspection of Finances is by law required to monitor spending by the COVID Fund. An audit was done focusing on spending in support of employment preservation, the operation of cash transfers to the informal sector, and the ministry of health. Staff had completed the standard safeguards assessment, a diagnostic review of the central bank's governance and control framework, in 2019.

43. **Relations with partners.** Fund staff working on Morocco have had long-standing and close coordination with their counterparts at the World Bank, which also provided substantial COVID-related assistance to Morocco.[19] They also discussed the conditions in Morocco with various other official lenders.

V. TUNISIA

When the pandemic hit, Tunisia had an EFF that was going to expire soon. However, that EFF was canceled and the Fund supported Tunisia through an RFI of 100 percent of quota (about US$750 million) instead. Staff-level agreement on a new EFF was reached in October 2022.

A. Background and Economic Developments

44. **Initial conditions.** Tunisia had been experiencing deep economic difficulties since the Arab Spring of 2011. Following a series of political and economic shocks, and delays in implementing needed reforms, major economic imbalances increased. Since 2010, growth rates declined, inflation rose steadily, and unemployment and poverty rose. To address social concerns, the role of the state in the creation of employment and provision of subsidies expanded. Fiscal deficits grew and public and external debt rose substantially after 2011. The BOP also weakened sharply. The Fund supported Tunisia through a series of programs that helped contain the macroeconomic imbalances, though with mixed results. The economy was already weak at the outset of the pandemic (Table 4). In 2019, growth was low, public debt was 72.3 percent of GDP, mostly in foreign currency; external debt was 90.3 percent of GDP. But inflation and the budget deficit were declining—albeit from high levels—and the external position was improving somewhat.

45. **Impact of the pandemic.** Tunisia quickly put in place containment measures such as the closure of maritime borders, restrictions on air travel, and isolation measures. Economic activity suffered from declines in tourism and exports. In April 2020, output was projected to contract by

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[19] Morocco already had a Disaster Risk Management Development Policy Loan with the World Bank that had been approved in December 2019 and could be restructured to provide quick financial support. The Bank further committed in December 2020 to support Morocco with a COVID-19 emergency response project in the amount of US$400 million. During calendar years 2020 and 2021, the Bank committed to provide a total of about US$2 billion to Morocco in all forms of financing.

4.3 percent in 2020, but the pandemic's impact was much worse than expected and the economy shrank by 9.3 percent (see Table 4). The current account deficit was much smaller than expected, however, partly because imports fell sharply; on the positive side, remittances increased. Political uncertainties about the formation of a government also contributed to the economic downturn.

Table 4. Tunisia: Selected Economic Indicators

	2019	2020				2021		
	Actual[1]	Projections Pre-COVID[2]	Projections COVID[2]	June WEO	Actual[3]	Projection Pre-COVID	June WEO	Actual[3]
GDP growth (Percent)	1.0	1.5	-4.3	-6.8	-9.3	2.9	3.6	3.1
Inflation (Percent)	6.7	5.3	6.2	6.1	5.6	5.2	5.3	5.7
Budget balance (Percent of GDP)	-3.9	-2.9	-4.3	-4.4	-9.8	-2.3	-2.5	-7.7
Government debt (Percent of GDP)	72.3	76.1	88.5	87.3	89.7	81.9	89.7	82.0
Current account balance (Percent of GDP)	-8.8	-8.0	-7.5	-8.8	-6.8	-8.3	-8.4	-6.2
External debt (Percent of GDP)	90.3	90.1	109.9	107.4	96.5	105.4	115.4	85.1
Official reserves (USD billions)	7.4	7.4	6.5	6.0	9.1	6.4	6.3	8.7

[1] Staff Report for the 2021 Article IV Consultations (IMF Country Report No. 21/44, February 2021).
[2] Staff Report for RFI (IMF Country Report No. 20/103).
[3] IMF WEO 2021.

46. **Policy response.** Although fiscal space was small, the government announced an emergency spending package of 2.3 percent of GDP, part of which was included in the 2020 budget. Spending on health supplies and equipment, strategic food reserves, income support was increased by 1.3 percent of GDP.[20] Firms were supported through tax relief, credit, and interest subsidies for affected sectors. The budget deficit was projected to increase to 4.3 percent of GDP, instead of falling to 2.9 percent as envisaged before the pandemic. The central bank lowered interest rates and encouraged deferment of bank debt servicing. The 2020 fiscal outcome, a deficit of nearly 10 percent of GDP, was twice as large as anticipated in April, driven by lower-than-expected GDP growth, higher transfers and subsidies, and capital spending.

B. Engagement with the IMF

47. **EFF replaced with RFI.** When the pandemic hit, Tunisia had an EFF with the Fund. But the authorities and staff agreed that a UCT program was not implementable in the face of the pandemic and so the EFF was cancelled two months before expiry. In its place, the Fund supported Tunisia through an RFI purchase in April 2020. Agreement on the RFI, in the amount of about US$750 million (100 percent of quota or 2 percent of GDP), was reached less than three weeks after the Fund received Tunisia's request. The budget financing needs, together with

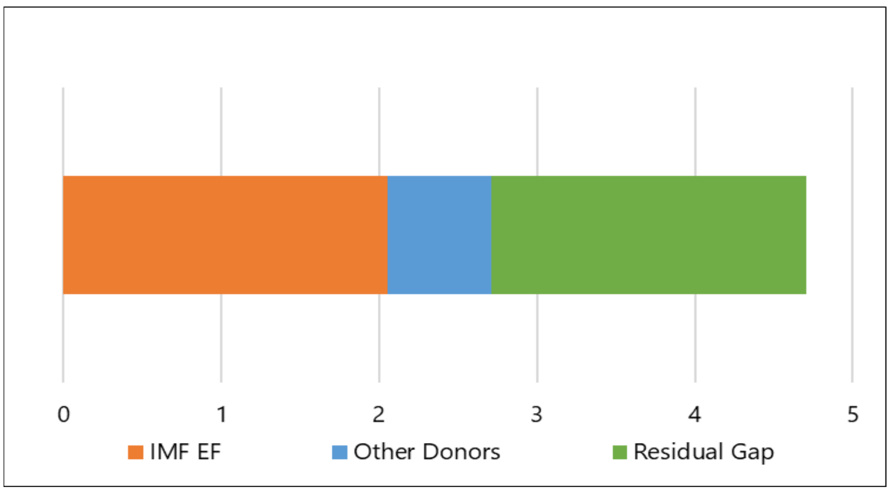
[20] See IMF Country Report No. 20/103.

developments in the external accounts, created a large balance-of-payments need estimated at US$1.7 billion (4.7 percent of GDP) at the time of the RFI request. Though the IMF provided the maximum access level, there was an unmet financing gap even after taking into account "identified financing from Tunisia's other external partners" (Figure 2).

48. **Policy commitments in the LOI.** The authorities' LOI incorporated policy commitments that would have likely been included in a UCT program. To defray the costs of the anti-pandemic measures and enhance public debt sustainability, the government agreed to take several measures, including adopting an automatic price formula for some fuels and lowering the civil service wage bill slightly. There were also commitments to lower energy subsidies and raise the price of natural gas, though these were not fully implemented. The central bank agreed to tighten if inflation picked up or depreciation expectations rose. It also agreed to a constrained intervention policy and to consult with staff if there were exchange rate pressures. Furthermore, the central bank agreed not to relax prudential banking regulations to combat the crisis.

Figure 2. Tunisia: Ex Ante Balance of Payments Gap, 2020

(Percent of GDP)



Sources: Staff Report; IEO staff calculations.

Note: Following Kincaid, Cohen-Setton and Li (2023), reserve drawdown is treated as financing.

C. Assessment

49. **Overall assessment.** The program was successful in providing resources to Tunisia amid domestic political divisions and stresses, global economic uncertainty, and donor hesitancy. As in the case of other countries, the staff felt under pressure to support Tunisia very quickly and that the Fund had to lead other international partners. Given Tunisia's difficult and long-standing economic problems, consideration was given to a new EFF program. However, this approach was not pursued in view of the prevailing political divisions and instability in Tunisia, the lack of a credible plan by the authorities to adequately address prevailing macroeconomic imbalances, and the importance of ensuring a quick provision of Fund assistance and encouraging other official financing. Access was another consideration in selecting an RFI: Tunisia would have likely

obtained less financing under an EFF first tranche compared with an RFI. In interviews, the authorities noted that the absence of ex post conditionality was instrumental in allowing agreement on Fund financial support during the pandemic. Staff were concerned that further financing without conditionality would weaken the economy, erode fiscal space, and threaten external stability, and indicated that a new EFF would need to follow the RFI to lower economic imbalances and risks. After lengthy discussions, staff-level agreement on a new EFF was finally reached in October 2022, although Executive Board approval of the program is still pending.

50. **Access levels and policies.** Prior to the pandemic, the staff thought that Tunisia needed drastic policy reforms, supported by a UCT program to address macroeconomic imbalances and structural impediments to growth. Under the conditions of the pandemic, however, they agreed to an RFI purchase, and endorsed the authorities' loosening of policies. Though the maximum access was granted, and the RFI helped fill most of the uncovered fiscal needs, there was still a large residual external financing gap. The Office of the Executive Director for Tunisia appreciated the help provided to the country but believed that the resources made available by the Fund to Tunisia were inadequate compared to needs. However, given the access limits on EF, it was not possible to provide more assistance to Tunisia without a new fully developed UCT program, particularly given concerns about the high external debt level and the weak track record of policy implementation.

51. **Relations with partners.** The IMF country teams had close working relations with the partner institutions and donors. The RFI did help the country's case with other official lenders, though they remained somewhat hesitant in their commitment in 2020 given political uncertainties and concerns about policy implementation. For instance, at the time of the formulation of the RFI, the Bank committed to providing US$184 million and US$500 million in 2020 and 2021, respectively, totaling less than the IMF disbursement in 2020 of about US$750 million.

52. **Debt sustainability.** The sharp economic downturn and the financing needed to address the pandemic raised the already high risks to the sustainability of public and external debt. Public debt was considered by staff pre-pandemic to be sustainable but—given the significant risks—only if strong policies were implemented and there was continued access to concessional financing. External debt was judged to be "resilient to shocks, except for exchange rate depreciation." Should there have been a pre-emptive debt restructuring? Seeking debt restructuring during the pandemic would have been highly disruptive. The approach taken was in line with the forbearance generally shown by the Fund during the pandemic in its judgments about sustainability: Tunisia's debt was judged to be sustainable, partly on grounds that most of the debt was owed to official creditors and that the risks to sustainability from exchange rate depreciation were contained by the closed capital account.

53. **Governance safeguards.** The RFI did not include any particular safeguards on the use of resources for anti-pandemic purposes, reflecting the lack, in the early stages of the pandemic, of established guidance on how these should be designed. With the development of Fund-wide COVID-related governance safeguard policies, the staff discussed safeguards with the authorities during the 2021 Article IV discussions, and the authorities agreed to undertake several actions.

These included an audit of the public-private COVID-19 fund, and publication on a government website of pandemic-related procurement contracts, including the beneficial owners. The staff recommended a full ex post audit of crisis-related spending after the end of the fiscal year. In interviews staff stressed the need for effective implementation of the agreed measures.

54. **Staff analysis and projections.** The shock to the economy was much larger than staff projected in April 2020. First, the economic contraction was much deeper—the output decline was the largest among MCD countries. This was due partly to resurgence of infections after a relaxation of anti-pandemic restrictions following early success in containing the spread. Political uncertainties about the formation of a government also contributed to the economic downturn. Therefore, 2020 growth projections were repeatedly revised down. The current account outcome, however, was slightly better than anticipated, partly because remittances were larger than expected. More importantly, the capital account did considerably better than expected with respect to short-term inflows. The budget deficit was also much larger than expected due mainly to higher spending on salaries and crisis response measures, and capital outlays. The staff were aware of the uncertainties around their projections.

VI. UZBEKISTAN

Uzbekistan received IMF emergency assistance in May 2020 under an RFI-RCF blend for a total US$375 million (50 percent of quota). There have been no discussions of a follow-up UCT program.

A. Background and Economic Developments and Fund Engagement

55. **Initial conditions.** Uzbekistan was a late starter to structural reforms but in the years before the pandemic had begun to credibly undertake reforms to move away from state-led growth and to ease distortions. Steps were taken to improve institutions, economic policymaking, and encourage private-sector growth. Ambitious and credible reforms were directed especially at liberalizing the trade and exchange regimes, improving the tax system and the financial system. Nevertheless, considerable reforms were still needed, including to the public enterprise system and labor regulations.[21] Prior to the pandemic the economy was in good shape. In 2019, GDP grew by 5.8 percent and inflation was 14.5 percent (Table 5). There was considerable consensus between the authorities and the staff on macroeconomic policies. The budget deficit, including policy lending to state enterprises, was 3.9 percent of GDP. Public debt was moderate, but external debt was rising on account of borrowing to finance capital spending. Official reserves, including those of the sovereign wealth fund—the Fund for Reconstruction and Development (FRD)—were comfortable. Bank credit growth was high.

56. **Impact of the pandemic.** As the pandemic broke, the authorities quickly introduced restrictions on movement and limited economic and social activity. Nonessential businesses were closed. With these measures and with the drop in external demand, depressed gas export prices,

[21] See the 2019 Article IV consultation report (IMF Country Report 19/129).

and lower remittances, the economy was projected to weaken in 2020 but growth was still expected to remain positive (Table 5). In the event, GDP grew by 1.9 percent, slightly better than projected in the RFI. The services sector was hit hard but the higher prices of gold, Uzbekistan's largest export, helped cushion the economy. The current account deteriorated, but much less than anticipated under the RFI (to 5.0 percent of GDP vs. the expected 9.6 percent) largely owing to import compression. Financial inflows and official reserves did much better than expected.

Table 5. Uzbekistan: Selected Economic Indicators

	2019	2020				2021		
	Actual[1]	Projections Pre-COVID[2]	Projections COVID[2]	June WEO	Actual[2]	Projection Pre-COVID	June WEO	Actual[2]
GDP growth (Percent)	5.8	6.0	1.5	1.5	1.9	6.0	7.0	7.4
Inflation (Percent)	14.5	13.8	12.9	12.9	12.9	10.6	9.5	10.8
Budget balance (Percent of GDP)	-3.9	-1.9	-5.6	-3.9	-2.5	0.3	-1.5	-4.6
Government debt (Percent of GDP)	28.3	29.7	34.5	35.4	37.6	24.8	35.8	36.8
Current account balance (Percent of GDP)	-5.8	-4.7	-9.6	-9.6	-5.0	-4.8	-7.9	-7.0
External debt (Percent of GDP)	43.9	41.7	46.3	47.8	58.3	32.4	48.4	60.0
Official reserves (USD billions)[4]	29.2	32.1	27.7	28.5	34.9	27.6	28.4	35.1

[1] 2021 Article IV Staff Report (IMF Country Report 21/85).
[2] RCF/RFI Staff Report (IMF Country Report 20/171).
[3] IMF WEO 2021.
[4] Includes foreign reserves for the Fund for Reconstruction and Development.

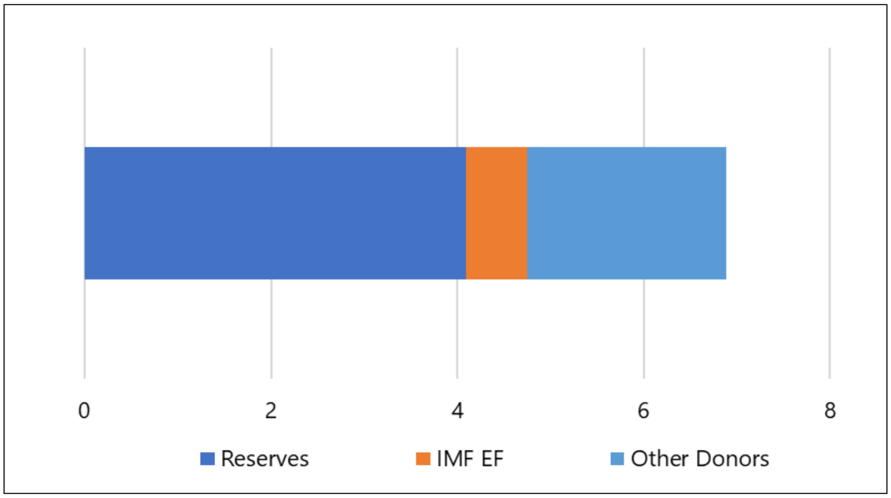
57. **Policy response.** The government promptly loosened the fiscal stance, putting in place a large spending package, much of which was disbursed through an anti-crisis fund. The package raised health spending, boosted transfers to low-income families, provided interest subsidies to businesses, financed public works, and provided tax relief. Health and social safety net spending rose by 0.4 percentage and 0.8 percentage points of GDP, respectively. But coverage of vulnerable households remained poor, owing to gaps in the safety net. Given the constraints on domestic budget financing, including on central bank financing, and an increase in sovereign bond spreads, fiscal financing was provided by FRD, IMF, and bilateral resources. Monetary policy was eased, helped by falling inflation. In addition to lowering its financing rate and providing short-term liquidity to banks, the central bank allowed some exchange rate flexibility, and the currency depreciated moderately.

B. Engagement with the IMF

58. **RCF/RFI.** Staff thought that external finance was necessary to finance the larger budget deficit and meet BOP needs, especially given the limited scope for the government to tap domestic financial markets. The Fund provided Uzbekistan with a package of US$375 million (50 percent of quota, of which 17 percent of quota was under the RCF with the remainder under

the RFI). Multilateral development banks and bilateral partners also contributed and the program was fully financed (Figure 3).[22] Staff and authorities indicated that 50 percent of quota—below the 100 percent cap—was regarded as sufficient to meet external financing needs. The authorities also raised US$750 million through Eurobonds, catalyzed by the RFI.

Figure 3. Uzbekistan: Ex Ante Balance of Payments Gap, 2020
(In percent of GDP)



Sources: Staff Report; IEO staff calculations.
Note: Following Kincaid, Cohen-Setton and Li (2023), reserve drawdown is treated as financing.

59. **Policies.** In the RCF/RFI request, the pandemic was characterized as a temporary shock not requiring drastic policy changes. Since Uzbekistan already had some policy space when it entered the pandemic, staff were supportive of the authorities' policies and thought that a temporary hike in the deficit would not harm fiscal sustainability. However, social safety net spending was relatively modest. They also concurred with the authorities' monetary easing and liquidity support to the banks. The staff also thought that no major policy adjustments were necessary in the short term to address the BOP difficulties. The authorities indicated that they would continue with structural reforms despite the crisis.

60. **Governance safeguards.** In the letter of intent, the government agreed to publish reports on pandemic-related outlays by the anti-COVID Fund on the Ministry of Finance website, and to publish procurement contracts, including the names of companies involved.[23] They also agreed to undertake independent audits of pandemic-related spending and publish the results.

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[22] During calendar years 2020 and 2021, the World Bank committed to provide Uzbekistan with US$1.8 billion.

[23] The Anti-Covid Fund was closed at end-2020 and the publication of pandemic-related spending was stopped. The authorities have been working with EBRD to set up an on-line platform with procurement data.

C. Assessment

61. **Overall assessment.** Uzbekistan and Fund staff had been working closely on the country's reform program and policies. With the onset of the pandemic, the staff agreed with the authorities on a temporary increase in the fiscal deficit and their approach to financing it. In retrospect, the policy response appears to have been a success: although the hit to economy was substantial, it still grew in 2020; and the authorities' credibility among donors and markets was sustained, enabling it to continue to borrow, and official reserves rose significantly rather than declining as foreseen under the program.[24] In 2021, the economy rebounded, with growth reaching 7.4 percent, though inflation remained high at 10 percent.

62. **Need for Fund financing?** Unlike the three case studies discussed above, there is a question whether IMF financial support was necessary in this case. Official reserves, including FRD reserves, were sizable, and Uzbekistan had some policy space. However, the Fund's decision to support Uzbekistan could be justified by the uncertainty about the course of the pandemic and its economic impact, the potential catalytic effect of Fund financing, as well as the small risks to the Fund's balance sheet due to the country's strong capacity to repay. The agreement to limit access to well below the available ceiling seems reasonable, leaving the possibility of a further drawing if needed if conditions deteriorated. The rebuilding of buffers and the authorities' reform orientation also appears to explain the lack of a need for a follow-up Fund program. Indeed, in retrospect, it could be argued that access could have been even lower given the size of Uzbekistan's reserves. However, the access level of 50 percent of quota was small relative to the size of the economy (0.6 percent of GDP), and Fund support helped catalyze financial resources from other official and private sources.

63. **Analysis and projections.** The staff expected the economic downturn to be short-lived, with growth resuming strongly in 2021. In the event, growth resumed in the second half of 2020, the balance payments situation proved better than envisaged, and official reserves rose significantly. Uzbekistan's external and public debt were judged by staff in 2020 to be sustainable, with low risk of debt distress.

64. **Implementation of governance safeguards.** Measures committed at the time of the EF request were subsequently implemented. The authorities confirmed that they had conducted audits by the chamber of accounts and published them in May 2021. The anti-COVID Fund provided daily reports on spending, including on beneficiaries. There was also an open-budget platform that was used to publish procurement contracts.

[24] Some of the increase in official reserves was because of the increase in gold prices.

VII. CONCLUSIONS

65. **Appropriate pivot in surveillance.** Staff's initial worries about the region were centered around the sharp spike in global risk aversion—portfolio flows to the region declined by nearly US$2 billion in February–March—and tightening financial conditions, seen as particularly challenging given US$35 billion in maturing sovereign debt in 2020. However, as concerns about the possible health consequences from the pandemic became more prominent in the region, the policy imperative pivoted to healthcare and humanitarian considerations. The April 2020 REO emphasized the immediate priority of containing the spread of the virus and advocated fiscal easing to accommodate necessary spending, a message reiterated by the MCD Director in his interactions with officials and in press interviews.

66. **Lending—successful triage.** At the onset of the pandemic, MCD senior staff quickly clustered the 32 countries in their region into a group of 12 countries that would not have need for EF from the Fund and a group of 5 countries (Iran, Lebanon, Libya, Sudan, and Syria) where providing access would be difficult for various reasons. By June 2020, the remaining 15 countries had received emergency or upper credit tranche (UCT) financing from the Fund, increasing the Fund's financing exposure to the region by more than 65 percent in 2020.

67. **Effectiveness of emergency financing.** Our case studies of Kyrgyz Republic, Tunisia and Uzbekistan paint a positive picture overall of the value to countries of the rapid provision of Fund EF. The first two received the maximum permitted under Fund access limits despite concerns about policies. Table 6 summarizes the amount of financing received by our case studies.

- **Kyrgyz Republic:** The support from the IMF helped Kyrgyz Republic allay the economic consequences of the pandemic. The speed of support and absence of conditionality were very much appreciated by the authorities and helped improve the sometimes-uneasy relationship with the authorities. The total amount of IMF support may have been small relative to the scale of the shock, but the authorities were not inclined to pursue a UCT program that would have been needed to justify higher UFR.

- **Tunisia:** Fund support was useful in providing resources to Tunisia amid domestic political divisions and stresses, global economic uncertainty, and donor hesitancy. Reaching the judgment that Tunisia's debt was sustainable required some 'forbearance' on the part of staff, in line with the general approach taken by the Fund during the pandemic (Kincaid, Cohen-Setton, and Li, 2023). The authorities noted that the absence of ex post conditionality was instrumental in allowing agreement on Fund financial support. Nonetheless, given the daunting reforms that were needed and the significant risks to debt sustainability, staff pressed for a new EFF to follow the RFI. After lengthy discussions, agreement on a new EFF was finally reached in October 2022.

- **Uzbekistan:** Unlike the two previous cases, there is a question whether IMF financial support was necessary in this case. Official reserves were sizable, and Uzbekistan had some policy space. However, the Fund's decision to support Uzbekistan could be justified by the uncertainty about the course of the pandemic and its economic impact, the potential catalytic effect of Fund financing, as well as the small risks to the Fund's balance sheet due to the country's strong capacity to repay. The agreement to limit access to well below the available ceiling seems reasonable, leaving the possibility of a further drawing if needed if conditions deteriorated. Indeed, in retrospect, it could be argued that access could have been even lower given the size of Uzbekistan's reserves. However, the access level of 50 percent of quota was small relative to the size of the economy (0.6 percent of GDP).

Table 6. Access and External Indicators

Member	Instrument Type	Amount of Emergency Financing/Debt Relief Received			Rank on Transparency International CPI, 2019	Overall Risk of Debt Distress, 2019	Global Health Security Index, 2019[1]
		USD millions	Percent of GDP	Percent of quota			
Kyrgyz Republic	CCRT	12.5	0.1	N/A	30	Moderate	43
	RCF	80.7	0.9	33.3			
	RFI	161.3	1.8	66.7			
Morocco	PLL	2970.0	2.5	240.5	41	N/A	35.6
Tunisia	RFI	745.0	1.9	100.0	43	N/A	32.1
Uzbekistan	RCF	125.0	0.2	16.7	25	Low	37.7
	RFI	249.3	0.4	33.3			

Sources: IMF; Transparency International (2019); Global Health Security (GHS) Index.
[1] Score is based on a scale of 0 to 100, where 100 = best health security conditions.

68. **Calibration of access levels under emergency financing.** The Kyrgyz Republic and Tunisia received the maximum permitted under Fund access limits despite concerns about policies and political developments that could have impinged on the capacity to repay the Fund. In the future, the Fund could consider a more tiered approach such that countries with particularly high risks could be kept to lower tier access below the standard ceiling, until such risks were adequately addressed.

69. **Successful PLL for Morocco.** The PLL worked as intended by helping a country with a solid policy framework and track record weather a large external shock through ready, rapid access to Fund resources without conditionality or protracted discussions on policies. The PLL also helped Morocco regain capital market access. The early repayment by Morocco highlighted one possible shortcoming of the PLL as part of a pandemic response, namely its high cost. Officials expressed concern about the Fund's high surcharge rates, suggesting that their use to support the Fund's income conflicted with the role of the Fund in providing financial support to its membership. Nevertheless, the authorities' regarded their overall experience with the PLL as very positive.

70. **Difficult cases.** Iran has been one of the countries most affected by the health consequences of the pandemic. The authorities requested in March 2020 US$5 billion in emergency assistance under the RFI to help address the health and economic impact of the pandemic. Thus far, Iran has not yet received a definitive response from the Fund. The Iranian authorities have repeatedly criticized the Fund for discriminating against Iran for political considerations.

71. **Governance safeguards.** The case studies clearly illustrate the growing attention over the course of the pandemic to governance safeguards. The March LOI for the Kyrgyz Republic—the first country to access Fund EF during the pandemic—included only commitments to conduct an ex post audit of the procurement of emergency medical supplies; while Kyrgyz Republic had well known governance issues, the Fund did not require steps to provide stronger safeguards at this stage. Tunisia's RFI also had limited commitments in this regard. Governance safeguards were strengthened over time but monitoring of implementation will remain a challenge.

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