IEO
Independent Evaluation Office
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BACKGROUND PAPER

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The IMF's Engagement with European Countries During the Pandemic

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The IMF's Engagement with European Countries During the Pandemic[*]

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ABBREVIATIONS

ARA	Assessment of Reserve Adequacy
BiH	Bosnia and Herzegovina
BOP	Balance of Payments
EBRD	European Bank for Reconstruction and Development
ECB	European Central Bank
EF	Emergency Financing
EIB	European Investment Bank
ESM	European Stability Mechanism
EUR	European Department (IMF)
FBiH	Federation of Bosnia and Herzegovina
GDP	Gross Domestic Product
IFI	International Financial Institutions
LOI	Letter of Intent
MFA	Macro-Financial Assistance
MoU	Memorandum of Understanding
RCF	Rapid Credit Facility
REO	Regional Economic Outlook
RES	Research Department (IMF)
RFI	Rapid Financing Instrument
RS	Republika Srpska
UCT	Upper Credit Tranches
WEO	World Economic Outlook

EXECUTIVE SUMMARY

This paper assesses IMF engagement with countries in the European Department (EUR) over the period January 2020 to April 2021, first describing the overall engagement with the region and then providing more detailed case studies on the experience of two countries (Bosnia and Herzegovina (BiH) and Kosovo) that received emergency financing (EF). The experience of two other countries (Belarus and San Marino) that were interested in access to EF but did not receive it is also briefly discussed.

Enhanced cross-country surveillance. While advanced economies in Europe did not have need for the IMF's financial resources, they benefitted from intensified and more cross-country surveillance efforts, mitigating the effects of the temporary suspension of Article IV consultations.

Limited but rapid emergency financing. The region's take-up of Fund emergency financing was limited (six countries, accounting for about $1.1 billion out of a global total of $31.8 billion), partly because many countries had other sources of support, including from European Central Bank swap and repo lines. EF was negotiated and disbursed quickly and viewed by staff as having a salutary effect on perceptions of the Fund within the region, especially given some delays in disbursements from other sources.

Collaboration and catalytic effect. Relations with other International Financial Institutions (IFIs), especially the European Union (EU) and World Bank (WB), were effective at the level of country teams. Despite the absence of conditionality, the macro framework and the debt sustainability assurances associated with the provision of IMF emergency financing were useful in facilitating financing from other official and private sources.

Complex considerations on access. Access usually was provided up to Fund-wide limits but there were also some departures. Kosovo's access was held at 50 percent of quota on concerns about political stability, though BiH received 100 percent of quota despite political concerns, illustrating that access depends in part on staff's judgments on how political developments are likely to impact polices and hence impinge on capacity to repay the Fund. Staff reluctance to provide EF to Belarus and San Marino was understandable given Belarus's unwillingness to follow health policies regarded as needed to contain the spread of the pandemic and the organization of mass gatherings universally seen as counterproductive, and San Marino's debt, which staff had assessed to be unsustainable in the 2020 Article IV consultation immediately before the pandemic struck. Nevertheless, both countries were in evident need and staff and the authorities agreed that Fund financing would have helped them overcome the effects of the pandemic.

Lessons. While timely support without conditionality was valued under the particular circumstances of the pandemic, some consideration could be given to whether, in future crises, some degree of conditionality might help countries' medium-run prospects without jeopardizing immediate needs to mitigate the effects of the crisis. Specifically, consideration could be given to the suitability of a more tiered approach, with quick initial access followed by further access once policy conditions are met. Tiered access could also help provide at least some support in very difficult cases, holding out the possibility of further access with progress on policies.

I. INTRODUCTION

1. **Purpose.** This paper assesses the IMF's engagement with European countries during the COVID-19 pandemic, drawing on the experience of two countries that received emergency financing (EF)—Bosnia and Herzegovina (BiH) and Kosovo. Both were among the early recipients of EF from the Fund, but access levels differed (100 percent of quota in the former, but only 50 percent of quota in the latter), providing useful perspectives on the Fund's considerations on how much financing to provide. The paper also touches upon the experience of two countries (Belarus and San Marino) that would have liked to receive EF but did not because health policies in Belarus were judged to be inimical to battling the pandemic, while in San Marino's case debt was assessed to be unsustainable in early 2020. The paper also briefly describes the Fund's overall engagement with the region, including the European Department's (EUR) policy advice during the pandemic and the department's strategy for helping the region through balance of payments (BOP) financing.

2. **Evaluation period and sources.** The focus of the assessment is on the period from January 2020 to April 2021. For the four country cases, the narrative is based on interviews with the IMF mission chiefs during 2020–21, several country team members (including resident representatives), senior reviewers within EUR, and country authorities. Internal documents provided by EUR for the country cases were also consulted. In addition, we interviewed EUR senior staff who were involved in crafting the department's strategy and financing decisions, staff who put together EUR's Regional Economic Outlook (REO) reports, Executive Directors and their advisors, and European Union (EU) staff.

3. **Structure.** Section II summarizes developments in the region during the pandemic and EUR's response to help countries through policy advice and financing and includes boxes on Belarus and San Marino.[1] Sections III and IV present case studies of BiH and Kosovo, respectively, including an assessment of IMF performance in each case.

II. IMF'S ENGAGEMENT WITH THE REGION

A. Developments and Policy Advice

4. **Pre-pandemic economic situation.** Prior to the pandemic, the European region was experiencing a slowdown in activity that mostly mirrored the broader global weakness in trade and manufacturing (IMF, 2019b). A modest recovery was projected in 2020, reflecting relative strength in emerging Europe. With both activity and inflation expected to remain subdued, the EUR Fall 2019 REO recommended that monetary policy accommodative. Recommendations for fiscal policy were dependent on individual countries' fiscal space, but the REO emphasized the need for adhering to medium-term objectives, while still allowing fiscal policy to respond to cyclical fluctuations in activity. EUR's February 11, 2020 informal briefing to the Executive Board expanded on the themes of the Fall 2019 REO and contained no reference to the pandemic (and did not elicit any questions from Directors about the pandemic).

[1] The Fund's capacity development and technical assistance work during the pandemic are covered in a separate IEO evaluation (IEO, 2022).

5. **Onset of the pandemic and April 2020 outlook.** By March 2020, however, infection rates in Europe were rising rapidly, and economic activity was being severely affected, including because of widespread lockdowns.[2] The likely severity of the pandemic's macroeconomic impact was reflected in the April 2020 World Economic Outlook (WEO) forecast, which projected that region-wide gross domestic product (GDP) would fall by around 6½ percent in 2020 (Figure 1). This grim baseline forecast of a recession worse than that of 2009 (when European GDP declined by 4.7 percent) was in EUR's view subject to notable downside risks as the baseline scenario assumed that the major disruptions associated with lockdowns would be temporary and did not anticipate widespread balance sheet impairment.

6. **Forecasting process.** As in other area departments, staff who worked on the EUR REO report noted that there was greater recourse to top-down guidance from the Fund's Research Department (RES)—which has responsibility for putting together the WEO—than during past crises. Staff noted some other challenges in forecasting economic developments:

- First, the measurement of "potential output" was particularly murky given the extraordinary uncertainty about how long COVID-19 would last and how it would affect structural aspects of both the supply and demand sides of the economy. As a result, EUR could not rely as much on the usual methods used in the Fund to measure potential output. By mid-2020, RES revised its guidance on measurement of potential output during the pandemic.

- Second, scenarios were not debated across departments as much as they might have been in more normal times. The broad sense was that the question of which scenarios were most likely to be the best representation of events was not particularly important because the policy advice was more or less the same for all. Several EUR staff, however, felt that the assumptions underlying a few of the scenario analyses were so extreme that those scenarios were more time-consuming than useful in shaping the debate.

As in other area departments, time pressures meant that updates to forecasts of inflation and external balances received less attention than growth forecasts, affecting the consistency of forecasts.

7. **April 2020 policy advice.** Both the April 2020 REO and EUR's April 2020 regional briefing to the Board provided clear support to "the unprecedented [European] policy response," which was seen as "essential to save lives" and "critical to minimize potential balance sheet effects and thereby improve the prospect of an early recovery." The Fund viewed it as "critical to augment fiscal space by supplementing national efforts with European support." At this stage, staff was not favoring any particular option for European support,[3] but considered that "early action at the EU level 'was

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[2] The Oxford Stringency Index (Hale and others, 2020) increased to a level of around 70 about one month earlier than in the United States and peaked at a level of around 90 in April 2020.

[3] Options considered at that stage included making the European Stability Mechanism (ESM) the instrument of choice for crisis management, expanding the European Investment Bank's (EIB) balance sheet, introducing a pan-European scheme to support the unemployed or workers on reduced hours and an EU fund to finance healthcare costs, and proposals for coronavirus bonds issued by a supranational entity.

essential' to ensure that forceful policy actions in high debt countries do not lead to a rise in spreads that could destabilize the euro area." The Fund later supported the European Commission proposal in May 2020 to create a new instrument ("Next Generation EU") outside the EU budget and financed by EU bonds, stating that it would "represent a significant macroeconomic stimulus while alleviating medium-term constraints for high-debt countries." The Fund also supported policy interest rate cuts and the use of unconventional monetary policies by the European Central Bank (ECB) and other central banks in advanced Europe. It was, however, publicly reticent to express how it viewed the use of unconventional monetary policies by several central banks in emerging Europe (Loungani and others, 2023).

8. **Policy response by national governments.** In line with IMF advice, large fiscal policy measures were quickly introduced by European governments, estimated to average around 7.5 percent of GDP for advanced Europe and 4 percent for emerging Europe.[4] In advanced Europe, monetary policy was eased using both conventional and unconventional tools. By end-April 2020, several central banks in emerging Europe had also announced some form of government bond purchase program, including large ones in Croatia and Poland. Macroprudential measures were deployed to encourage continued bank lending. Steps were also taken to reduce supply-side disruptions, including job retention schemes to discourage workers from exiting the labor force, tax deferrals and other forms of financial support to prevent firm closures, as well as structural measures aimed at boosting longer term potential.

9. **Policy response by European institutions.** In addition to relaxing existing rules for fiscal policy and State aid, the EU mobilized supranational resources to finance new facilities and complement national fiscal policies. In April 2020, EU leaders approved €100 billion in loans to help protect jobs through job-retention programs; a €200 billion Pan-European guarantee fund, enabling the European Investment Bank (EIB) to increase support to firms; and a €240 billion European Stability Mechanism (ESM) precautionary credit line, to cover COVID-19-related healthcare costs (for up to 2 percent of GDP per country). In May 2020, the European Parliament approved a €3 billion macro-financial assistance (MFA) package to 10 enlargement and neighborhood partners to help them limit the economic fallout of the coronavirus pandemic. EU leaders also agreed on the €750 billion "Next Generation EU" package that provides a one-off augmentation of the EU budget to finance through a joint-bond issuance an ambitious program of investment and reform projects in EU member states over the period 2021–26, with €390 billion to be distributed as grants. For emerging Europe, policy space was boosted by the introduction of new bilateral swap and repo facilities by the ECB.

[4] These estimates were obtained by calculating the arithmetic average for each income group using the "Fiscal Monitor Database of Country Fiscal Measures in Response to the COVID-19 Pandemic," available at https://www.imf.org/en/Topics/imf-and-covid19/Fiscal-Policies-Database-in-Response-to-COVID-19.

10. **June 2020 revisions.** In June 2020, the IMF turned even more pessimistic about the growth prospects for the global economy, as discussed in Loungani and others (2023). A large decline in GDP—of 8½ percent—was projected region-wide in Europe for 2020 (Figure 1).[5] Several factors contributed to the downward revisions, including longer-than-previously-expected lockdowns and more pessimistic views about investment prospects. With infection rates appearing to have crested, the risks to the growth forecast were now viewed as being evenly balanced, with the danger of a renewed surge of infections matched by the possibility that re-openings could happen sooner than expected.

11. **Evolution of 2020 forecasts and advice:**

- By the time of the Fall 2020 WEO, when some early signs of recovery were appearing, EUR presented a somewhat less pessimistic view of the pandemic's macroeconomic effects, projecting a decline in region-wide GDP of 7 percent (Figure 1).[6] The department advocated continued fiscal and monetary policy support (the former especially targeted to vulnerable populations), with steps to encourage bank balance sheet repair, and active labor market policies to avoid unemployment becoming entrenched. The department also emphasized that a more focused approach was needed where fiscal policy space was limited.

- During the last three months of 2020, Europe experienced a second and even more severe wave of infections, although with lower mortality rates. Nevertheless, many economic indicators were showing signs of a strong recovery, with the rollout of vaccines in late 2020 and early 2021 and the easing of lockdown restrictions in early 2021 providing a further boost to confidence and economic activity. The Fall 2020 REO (IMF, 2020a) re-emphasized the "imperative to maintain policy support until the recovery is fully entrenched" and the risks associated with scaling support back prematurely. In addition, the department advised that the recovery be "backstopped by transformative policies that address medium-term challenges," using fiscal resources that would be freed from emergency support to sustain investment. In this light, the call for policy support became less focused on "whatever it takes" and more case dependent—i.e., while countries were advised to avoid a premature withdrawal of support, those with less fiscal policy room were advised to focus their efforts and seek international support.[7] More emphasis was also put on gearing policy responses toward minimizing the danger that unemployment become entrenched and ensuring that recovery initiatives also supported structural transformations that could boost underlying potential output and decrease the risks related to climate change. However, the department warned that recent efforts to provide liquidity support to firms may need to be re-oriented to addressing solvency shortfalls and/or facilitating debt workouts.[8]

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[5] The forecast for Advanced Europe was decreased from -7.3 percent to -9.8 percent. For Emerging Europe, the revision was lower going from -5.2 percent to -5.8 percent.

[6] The forecast for Advanced Europe was increased from -9.8 percent to -8.2 percent. For Emerging Europe, the forecast was increased from -5.8 percent to -4.6 percent.

[7] See also the EUR briefing to the Board on October 2, 2020 (IMF, 2020b).

[8] This issue was the subject of an analytical chapter in the October 2020 REO (IMF, 2020a).

Figure 1. Forecasts for EUR Real GDP Growth and Inflation in 2020–2021
(In percent)

Sources: IMF; IEO staff calculations.

12. **2020 outcomes.** The region's output decline in 2020 ended up at 5 percent, less severe than had been projected in June 2020 (see Figure 1). The contraction in Advanced Europe—almost 7 percent—was more severe than in Emerging Europe, perhaps because governments in the latter had more time to react to the delayed spread of the virus compared to Western Europe and many of the countries eventually implemented lockdown measures that were less stringent than those from the early part of the year (IMF, 2020a).

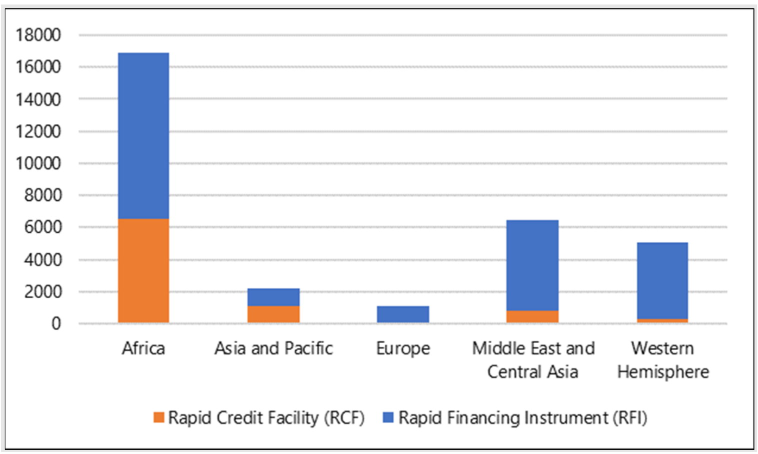
13. **2021 outlook and advice.** The European economy rebounded strongly in 2021 at a rate of almost 6 percent, regaining a large part of the 2020 output losses and requiring staff to revise up their 2021 growth forecasts (Figure 1). While welcoming the recovery, the Fund continued to warn against a premature withdrawal of policy support that could drag countries back into recession. By April 2021, the Fund's view was that "policies should continue to support activity" but also "transition from providing lifelines to facilitating the reallocation of labor and capital towards viable sectors." Both the global demand recovery and pandemic-induced supply disruptions contributed to higher-than-anticipated inflation of nearly 5 percent in 2021, a surge that was not anticipated by staff (Figure 1).

B. Strategy and Financial Support

14. **The Fund's emergency support to the region.**

- In response to the pandemic, the Fund quickly pivoted to providing financial support. According to EUR senior staff, the strategy was "to put money down as an anchor" as quickly as possible to create confidence and stabilize expectations. Emergency financing (EF) was seen as the "right tool" given that the pandemic was an "act of God" that did not require policy conditionality and provided enough time to prepare for more traditional upper credit tranche (UCT) arrangements down the line. However, the region's take-up of Fund EF was small compared to that in other regions (see Figure 2)—accounting for about $1.1 billion out of a global total of $31.8 billion—partly because many countries had access to other sources of liquidity support, including from the European Central Bank's swap and repo lines.

Figure 2. The Fund's Emergency Financing by Region
(In USD millions)

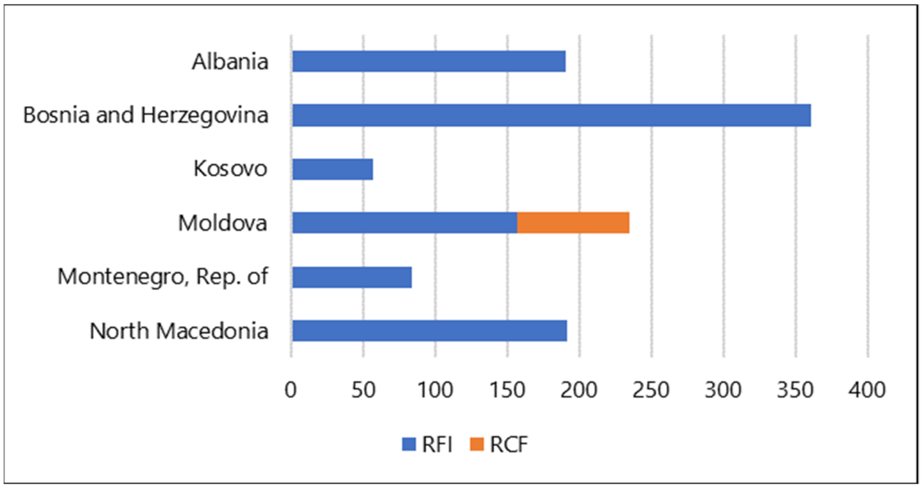


Sources: IMF; IEO staff calculations.

- In the end, six EUR countries (Albania, BiH, Kosovo, Moldova, Montenegro, and North Macedonia) received EF for a total amount of SDR 819 million (Figure 3), about 1.3 percent of the combined GDP of these countries (see Figure 3).[9] One of them (Moldova) transitioned to a UCT program of 232 percent of quota (about US$558 million or 4.6 percent of GDP) in December 2021. Ukraine also received additional Fund financing in June 2020 in the form of a UCT program for 179 percent of quota (about $US5 billion and 3.2 percent of GDP). Besides providing an important stopgap in the face of the withdrawal of international capital flows and the surge in public spending, staff viewed this support as having a salutary effect on perceptions of the Fund within the region, especially given multiple delays in the disbursements from other sources.

[9] Except for Moldova, which received one-third of EF through the Rapid Credit Facility (RCF) on concessional terms, all other EUR countries received EF through the non-concessional RFI.

Figure 3. The Fund's Emergency Financing in Europe
(In USD millions)



Sources: IMF; IEO staff calculations.

15. **Access decisions.** Consistent with the Fund's overall strategy, EF was negotiated quickly, and access was usually provided up to Fund-wide limits. Staff waited until annual access limits were increased from 50 to 100 percent of quota to submit the financing requests to the Board. This was seen as a pragmatic way to avoid returning to the Board twice in a short time window to obtain the full 100 percent of quota. The only exception was Kosovo, which—as further discussed in section IV—received Fund support of only 50 percent of quota as political instability caused Fund staff to take a cautious approach to financing. Two countries (Belarus and San Marino) were interested in EF access but did not receive it either because health policies were judged to be inimical to battling the pandemic (in the first case) or because debt was assessed to be unsustainable (in the second). Even in these countries where policy choices or debt sustainability concerns precluded emergency support, interactions with staff appeared positive (Boxes 1 and 2 discuss access decisions in these two cases).

Box 1. The Decision Not to Provide RFI Financing for Belarus

Belarus entered the pandemic with broadly stable economic conditions but significant vulnerabilities and structurally weak economic growth. Suspension of energy subsidies from Russia and heavy and inefficient state intervention in the economy left average GDP growth below 1 percent during 2015–19. Restrained macroeconomic policies maintained public and external debt in stabilizing ranges at 42 percent of GDP and 31 percent of GDP, respectively, at end-2019. However, staff viewed the country's long-ongoing discussions with Russia on compensating for the suspension of energy subsidies as unlikely to succeed, and, especially in that context, saw low official reserves (63 percent of the IMF's reserve adequacy metric) as a key vulnerability. Relations with the IMF were difficult, and multiple attempts to conclude a UCT arrangement had floundered.

Discussions on a RFI could not be concluded despite the country's evident need. Early indications were that the pandemic would take a large toll, with staff and the authorities agreeing that GDP would fall by about 6 percent in 2020. Mitigating fiscal measures were put in place in March to support businesses and people hurt by the drop in activity and to bolster the health system. Against the backdrop of a sharp fall in reserves in early 2020 and recognizing the potentially high cost of mitigation measures, the authorities approached the Fund for an RFI purchase in mid-March. Technical discussions with the staff during the following month produced agreement on some policies. Staff concluded that Belarus met the qualification criteria (specifically BOP need) for an RFI purchase of 100 percent of quota, but two issues of contention prevented agreement.

The issue that derailed the discussions was lack of agreement on virus containment interventions. A WHO mission to Belarus in mid-April to assess measures undertaken to contain the pandemic suggested that the authorities were flaunting safeguards employed in other countries. Such concerns were underlined by the organization of a mass gathering on May 8, an action seen by staff as incompatible with the goal of limiting the fallout from the pandemic, the very objective that the RFI was meant to support. Fund staff underscored the importance of conforming to WHO guidelines and insisted that language to that effect be included in the LOI. The authorities regarded public health measures as in the control of the President only and questioned why an agreement with the IMF should be based on such conditions.

A second difficulty was over the use of capital flow management measures (CFM). Staff wanted contingency plans to be prepared to deal with intensified capital outflows. Reserves were precariously low and another defense of the ruble would have lowered them to levels where capacity to repay the Fund would be in question. On a list of ten capital market management provisions under negotiation, nine were agreed. Disagreements on the tenth—related to restrictions on deposit withdrawal should the need arise—were not resolved before negotiations broke down over pandemic containment policies.

Informal contact between staff and the authorities continued through the year but without progress on an RFI.

In the end, Belarus managed to ward off threats to the outlook without IMF financing. Between May and September 2020, the authorities were able to obtain much-needed funding from the market, the World Bank and other sources (nearly US$100 million from the WB approved in May 2020 to support a specific health sector project, US$500 million from the Eurasian Fund for Stabilization and Development in October 2020, and later US$500 million from Russia in December 2020). Belarus also issued two Eurobonds in 2020; US$500 million in June and US$750 million later in the year at interest rates of about 6½ percent. The 2020 financing gap identified in April was amply filled through these sources, albeit at far greater cost in the case of the Eurobond. The effect of the pandemic on GDP turned out to be far smaller than projected and feared pressure on the currency was not so serious as to require activation of any CFM measures.

Authorities' views. Though funding turned out to be ample, the authorities felt that additional financing from the IMF could have been used to provide more support to households and/or reinforce the foreign reserve position. They also stated that the fact that they were in negotiations—even if inconclusive—with the IMF helped secure the issuance of the Eurobonds, though an RFI would have provided an even better signal for markets. Despite lack of agreement on an RFI, IMF staff's relations with the finance ministry and central bank remained cordial.

The question arises whether the IMF's withholding of RFI support was reasonable. Belarus presented an exceptional dilemma: should IMF resources intended to help countries put in place COVID mitigation measures without undue effects on reserves or debt be expended when the country's leadership refuse to implement containment measures that were near-universally regarded at the time as essential to suppressing the pandemic? Staff was also concerned about reputational risks if an RFI was approved in the absence of these policies.

Discussions over the RFI took place during a politically fractious time. A highly contentious Presidential election was due to be held in August 2020, and staff was aware that some commentators might view an RFI as indirectly funding the incumbents. Staff attests that political considerations were never part of the discussions with the authorities and that no political pressure was placed upon them in their recommendation to management not to provide EF support to Belarus.

The decision to make health policies a decisive consideration was novel, but had a compelling logic and was evenhanded. There was strong consensus at the time that containment measures were an essential part of mitigating the effects of the pandemic, and no other country that received EF followed such a hands-off approach to containment measures. It would be hard to call the link drawn between the lack of containment measures and—through its presumed effects on the economy—on the capacity to repay the Fund as unreasonable.

Box 2. San Marino—Debt Sustainability as an Impediment to RFI Support

Pre-pandemic conditions. San Marino entered the pandemic in a structurally weak position. GDP in 2019 was still below the pre-Global Financial Crisis level, reflecting effects of the crisis on offshore banking activity and slow recovery of demand for manufactured exports. The banking system, still reeling from the Global Financial Crisis, was undercapitalized despite periodic official support. A decade-long effort to achieve structural change that would establish sustainable growth had yet to be effective. This weak decade significantly narrowed the options for policy responses to mitigate the effects of the pandemic. As San Marino uses the euro as its currency, its meagre fiscal and banking buffers were a source of vulnerability.

2020 Article IV consultation. A consultation that judged public debt to be unsustainable had just been completed as COVID broke out. Staff concluded that, owing mainly to past and expected future official interventions in banks (especially to repair the balance sheet of the country's largest bank, Cassa di Risparmio di San Marino (CRSM)), implicit public debt had reached unsustainable levels. Staff strongly urged a recapitalization of CRSM with burden-sharing, while the authorities favored full recapitalization from the government. Staff also pointed to the absence of access to international financial markets as a vulnerability. Despite the outbreak of the pandemic, staff proceeded with publication of the Article IV report with these conclusions on debt sustainability.

Impact of the pandemic. The pandemic had a severe health and economic impact. The rate of cases and deaths in San Marino's first pandemic wave were among the most severe in Europe. Strict containment measures, the toll of illness on the domestic economy, and falling foreign demand resulted in a sharp drop in activity in Q2 2020. With tight limits on resources for fiscal support, the authorities were strategic in targeting support via direct transfers, a wage supplement scheme and health spending. However, cuts in some non-essential spending left the overall fiscal stance procyclical.

Engagement with the IMF. In informal discussions, staff and the authorities agreed on most aspects of the projections on the impact of the virus and the policies to respond to it. The tight constraints on resources for combatting the fallout from the pandemic were also commonly recognized. Reflecting very low bank liquidity, barely adequate international reserves, and potential weaknesses in the BOP, a substantial BOP need was identified. Nevertheless, with a clear judgement that public debt was unsustainable in the just-issued 2020 Article IV staff report—and a difference of view between staff and the authorities on how to attain sustainability—no progress could be made toward an RFI.

Outcomes. In mid-2020, San Marino received a €100 million repo line from the ECB. Later in the year, it secured a €150 million one-year bridge loan and then launched a Eurobond (3.25 percent yield) in early 2021. In late 2020, San Marino recapitalized CRSM, raising the public debt ratio to 78 percent of GDP. Accompanying measures to improve practices in the bank left the banking system in a much sounder condition.

Authorities' views. Though relations between the Fund and San Marino remain good, the authorities made several observations about their engagement during 2020. They understood that, with the 2020 Article IV Staff report issued, it was impossible for the Fund to consider an RFI despite the shared view on need. They, however, took issue with the Fund's methodology for judging debt sustainability for a very small and very open economy like San Marino. Moreover, they felt that access would not have had to be large to convey significant benefits as San Marino sought access to international markets.

16. **Precautionary arrangements.** Part of the Fund strategy was also to reach out and propose precautionary arrangements to EUR countries with strong policy fundamentals. In the end, no country made use of such an arrangement. Some simply did not have a BOP need. Others expressed interest in a Flexible Credit Line (FCL) or Precautionary Liquidity Line (PLL) arrangement. But in the end, this was not pursued by countries owing to concerns that they might not meet the eligibility criteria, that accessing PLL rather than FCL could be seen as a sign of weakness, and access to alternative sources of financing thanks to ECB liquidity and swap lines, as well as relatively low-cost borrowing from markets after the initial market turmoil receded.[10]

[10] ECB precautionary swap lines were agreed with Denmark (March 20, 2020), Croatia (April 15, 2020), Bulgaria (April 22, 2020). ECB repo lines were agreed with Romania (June 5, 2020), Serbia (July 17, 2020), Albania (July 17, 2020), Hungary (July 23, 2020), North Macedonia (August 18, 2020), and San Marino (August 18, 2020).

17. **Relationship with partner agencies.** In April 2020, the EU decided to expand the list of IMF instruments that qualified as a pre-condition for EU's MFA financing by including Fund EF.[11] As a result, all six cases of Fund EF in EUR were complemented by MFA financing from the EU.

18. **Surveillance.** Like other area departments, EUR put formal Article IV consultations on hold and instead intensified day-to-day monitoring and regular contacts. Virtual meetings with country authorities typically took place once a month to collectively try, as staff described it, "to get a handle on how bad things might get." Compared to normal times, surveillance efforts became more cross-country oriented and led by the department's front office with large intra-departmental teams drawn based on staff interest on topics like the impact of the pandemic on banks and corporates or the impact of lockdowns on economic activity (which became a chapter of the October 2020 REO). Senior EUR staff noted that there was more exchange of information with country authorities while the work was being carried out compared to normal times and that there was "huge appetite" for presentation of the work. Topics covered included: the specific fiscal support measures that were needed; how to support the corporate sector and small businesses; and what kind of labor market policies were best suited to the circumstances of the pandemic. Senior EUR staff noted that, paradoxically, "there may have been more surveillance going on after Article IV consultations were suspended." As noted by Loungani and others (2023), the policy trackers that the Fund introduced to summarize the key economic responses governments were well-received by the public and country authorities but staff complained that it was very stressful for country desks to fill out and update them regularly.[12]

III. Bosnia and Herzegovina

19. **Overview.** BiH experienced the pandemic in multiple waves. The first, when a strict lockdown was enforced, entailed a strong contraction in domestic demand and weakening exports. The second, starting in late 2020 brought larger case counts and intense strains on hospitals, and kept the recovery of domestic demand weak while external demand recovered. BiH's fragmented government structure—three entities, the Brčko District of BiH, the Federation of BiH (FBiH), and Republika Srpska (RS), with separate governments—has made agreement on and execution of IMF

[11] MFA is an instrument designed to provide loans and grants from the EU to candidate, potential candidate, and neighborhood countries in acute BOP crises. The Commission typically disburses MFA assistance in instalments strictly tied to the beneficiary country's progress with respect to macroeconomic and financial stabilization and economic recovery, implementation of the agreed policy reforms, as outlined in the Memorandum of Understanding, and sound progress with the IMF program, as indicated by successful reviews. The MFA lacks a framework regulation, which means that each individual MFA operation with a country in crisis requires a separate legislative decision. In the context of the COVID-19 crisis, a €3 billion MFA package for ten countries was adopted to speed the usual process. The legislation decision also deviated from the usual practice of requiring an UCT-quality arrangement and made MFA available to countries that benefited from IMF emergency funding.

[12] See https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19.

lending difficult, and the RFI was no exception.[13] Even without conditionality, the RFI faced obstacles in getting off the ground due to disagreements on the distribution of funds between the different entities.

A. Background and Economic Developments

20. **Initial conditions.** After several years of generally stabilizing macroeconomic policies, BiH entered the pandemic period with relatively strong fiscal and financial conditions. On the heels of several years of fiscal surplus, end-2019 public debt was 32 percent of GDP. The banking sector was adequately capitalized on average, and supervision and regulatory procedures were improving. Official reserves were above the IMF's Assessment of Reserve Adequacy (ARA) level; use of reserves was constrained by a currency board with the convertible marka (KM) fixed to the euro. Inflation was in low single digits.

21. **Structural impediments.** The longstanding problem for BiH was structural weaknesses that held back employment growth and infrastructure investment. Estimated potential growth (about 3 percent) was low among Western Balkan countries. A three-year Extended Fund Facility (EFF) to address these structural weaknesses started in 2016 but floundered before the second review could be completed. The authorities announced policies inconsistent with the program objectives and there were delays in forming the State government following elections in 2018. Although the arrangement had been extended to September 2020, it was canceled in April 2020 because the RFI would have exceeded the cumulative access limit (which includes committed but undisbursed amounts).

22. **Impact of COVID-19.** A strict lockdown, imposed soon after the early 2020 outbreak of COVID in Italy, was successful in containing cases and deaths. Together with external market disruptions (affecting merchandise exports, remittances, and tourism), the severity of the lockdown was expected to take a heavy economic toll. Projections for the RFI were built on the assumption that a recovery would begin only in late 2020. In the early April RFI request document, 2020 GDP was projected to fall by 5 percent. Despite supply disruptions, the CPI was expected to fall slightly in 2020 and then return to low inflation (Table 1). The impact on the external position was projected to be similarly dramatic. A projected sharp drop in current account receipts was expected to push the current account deficit from around 3½ percent of GDP in recent years to 7½ percent of GDP. Conditioned on an easing of the pandemic by 2021, imbalances were expected to start returning to more normal levels.

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[13] In the 1995 peace agreement between warring factions, two "entities," FBiH and RS, were formed with separate governments and a weak overarching State government. A lack of political consensus among the dominant ethno-nationalist parties hampers reforms. The Brčko District of BiH was formed in 1999 to reflect the multi-ethnic nature of Brčko and the surrounding areas.

Table 1. Bosnia and Herzegovina: Selected Economic Indicators

	2019	2020				2021
	Actual[3]	Projections pre-COVID	Projections COVID[1]	June WEO	Actual[2]	Actual[2]
GDP growth (Percent)	2.8	2.6	-5.0	-8.0	-3.1	5.8
Inflation (Percent)	0.6	1.4	-0.6	-1.1	-1.1	2.0
Budget balance (Percent of GDP)	1.4	0.7	-4.4	-6.1	-4.7	-0.7
Government debt (Percent of GDP)	32.5	32.5	38.0	41.8	36.5	36.5
Current account balance (Percent of GDP)	-2.8	-4.9	-7.5	-6.7	-3.8	-2.4
External public debt (Percent of GDP)	64.3	62.8	72.4	75.6	64.4	63.6
Official reserves (Billions of USD)	0.6	N/A	0.6	N/A	0.7	0.8

Sources: IMF; IEO staff calculations.
[1] January 2020 WEO (IMF, 2020c); [2] Staff Report of Request for RFI (IMF, 2020e) and IMF 2022 Article IV (IMF, 2022b); [3] IMF Fall 2019 WEO (IMF, 2019a).

23. **Fiscal response.** Immediate fiscal measures in early 2020 increased spending on health services, the social safety net, and support for businesses. The drop in fiscal revenue stemming from the weakness of domestic activity was to be accommodated. The overall stance of fiscal policy met with staff approval, though in a later report, staff were concerned about insufficient targeting of spending. The fiscal deficit was projected to go from small surpluses in recent years to a deficit of 4½ percent of GDP in 2020 (Table 1). Although public debt would jump to 38 percent of GDP, a return to surpluses was expected to start in 2021 and put public debt below 30 percent of GDP by 2023.

24. **Other policies.** With a currency board and fixed exchange rate, monetary policy had little role to play. The authorities committed to maintaining the currency board and resisting political pressure to use central bank financing for the government. The authorities implemented a six-month framework for a moratorium on loan repayments to banks on a case-by-case basis. They also temporarily prohibited dividend and bonus payments by banks.

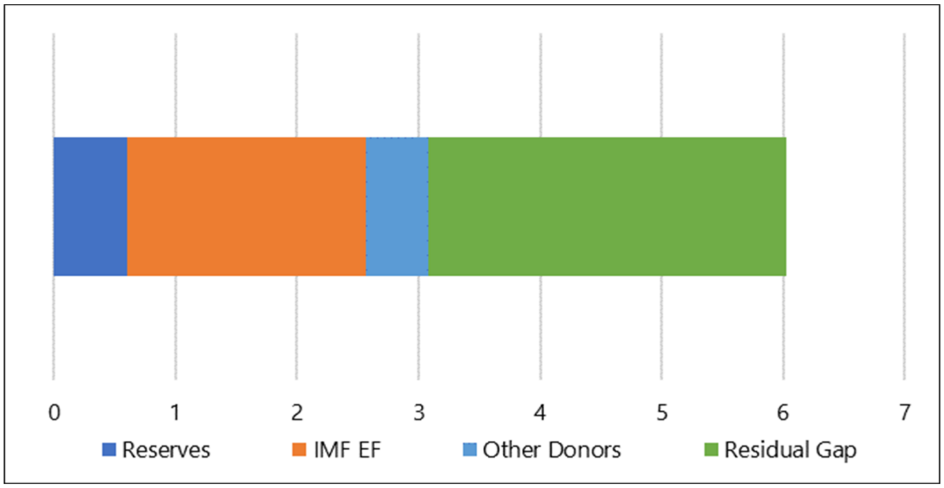
B. Engagement with the Fund

25. **External financing gap and access level.** The estimated external financing gap for 2020 was around 6 percent of GDP (Figure 4).[14] RFI financing at 100 percent of quota (or around 2 percent of GDP) would fill about one third of the BOP gap, while the EU, World Bank, other unidentified sources, and use of reserves would fill the remainder. Just under half of the gap was attributed to the public sector's financing requirement. IMF funding was on-lent to entity governments. Given the emergency nature of the assistance under the RFI, the BiH authorities decided to change the terms for

[14] This figure includes a projected drawdown in reserves of 0.6 percent of GDP. The staff report's headline estimate did not count the drawdown of reserves as a financing source. See Kincaid, Cohen-Setton, and Li (2023) for a discussion of the adjustment applied to staff estimates to obtain a harmonized and comparable measure of the BOP gap across staff reports.

distribution of funds between the entities used in the past for General Resource Account (GRA) purchases (for example, EFF-supported programs). Therefore, the RFI resources were credited to the entities (the Brčko District of BiH, FBiH and RS) only on June 3, 2020, following the ratification of the political agreement by the BiH Council of Ministers.

Figure 4. Bosnia and Herzegovina's Ex Ante Balance of Payments Gap
(In percent of GDP)



Sources: Staff Report (IMF, 2020e); IEO staff calculations.

26. **LOI commitments.** While there were no prior actions, the LOI included a commitment for the authorities to adopt a Deposit Insurance law and conclude a credit line with the European Bank for Reconstruction and Development (EBRD) to backstop the deposit insurance. Two other fiscal measures (adoption of the 2020 State budget and changes to tax laws in the Federation) were also included. The staff report also indicated that "it [was] unfeasible to complete a review or engage in discussions of a multi-year program at this juncture." However, the authorities expressed interest in a future EFF.

27. **EU and World Bank financing.** Early commitments of the World Bank and EU were delayed (or in the case of the EU incompletely disbursed) so that the Fund's financing represented about 90 percent of total official financing in 2020, and about half of the total for 2020–21. The decision by the EU to provide MFA to 10 enlargement and neighborhood partners in the context of the COVID-19 pandemic was adopted on May 25, 2020. Within that framework, a €250 million MFA loan was approved for BiH. The disbursement of the first instalment, however, only occurred in October 2021 as Parliaments only ratified in summer 2021 the Memorandum of Understanding, which laid out the specific policy measures that BiH would implement. These included measures to improve economic governance, financial sector stability, transparency and fight against corruption and a better functioning of the labor market. The disbursement of the second and final instalment of €125 million that was conditional on the implementation of these policy measures was cancelled as BiH did not

fulfill seven of the nine conditions laid out in the Memorandum of Understanding (MoU).[15] In addition to the MFA, the EU also provided €95 million in grants to support the country in its fight against the COVID-19 pandemic.[16] The World Bank approved an Emergency COVID-19 project in April 2020 for $36.2 million, but the disbursement occurred only in October 2020.[17] The Bank also approved a Firm Recovery and Support Project for micro-, small- and medium-scale enterprises affected by COVID-19 for $65.3 million December 2020; the first disbursement occurred in December 2021.[18]

28. **Follow-up UCT arrangement.** Talks on a follow-up EFF in late 2020 were unsuccessful. While broad understandings were reached on macroeconomic policies for 2021 as well as many structural reforms, negotiations stalled mainly because the RS authorities refused to implement reforms including some from previous Fund arrangements that would reduce the fragmentation of the economy, increase integration of entities in the BiH economy, and strengthen country-wide institutions. While these reforms entailed no short-term economic costs, the RS considered them a politically unpalatable transfer of competencies to the center.

29. **Governance safeguards.** BiH's RFI was approved in early April, before the framework for governance safeguards in the context of the COVID-19 pandemic was fully developed (see Kincaid, Cohen-Setton, and Li, 2023). The authorities' LOI supporting the RFI request only included general commitments to overhaul the health sector, including tighter controls on spending and incentives for fiscal consolidation of the sector, with measures to be fully implemented in a successor UCT program. It did not include specific commitments related to the use of COVID-19 funds.

30. **Follow-up on safeguards.** While BiH authorities took certain measures including the 2020 Article IV consultation commitment to enhance transparency regarding pandemic related spending, BiH was seen by staff as falling short of the transparency measures implemented in other countries that received Fund EF. The 2020 Article IV concluded in February 2021 thus encouraged the authorities to enhance these measures, by extending the publication of the details of the awarded contracts for all COVID related spending awarded contracts along with the publication of the names of the beneficial owners of the entities that have been awarded the contract(s) (IMF, 2021b). The same encouragement was repeated in the 2022 Article IV (IMF, 2022b). Similarly, staff urged the authorities to enhance the quality of their audits. While FBiH audit institutions prepared an audit of COVID-related spending, the RS supreme audit institution only conducted a routine audit of overall government spending.

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[15] Georgia is the only other country whose second tranche of the MFA was not disbursed as the EU judged it to have reversed course on policy commitments of its MoU.

[16] The €95 grant is composed of €13.7 million for vaccines, €7.76 million for medical needs. €73.5 million to support the socio-economic recovery. See https://ec.europa.eu/commission/presscorner/detail/en/ip_21_5104.

[17] See https://projects.worldbank.org/en/projects-operations/project-detail/P173809.

[18] See https://projects.worldbank.org/en/projects-operations/project-detail/P174604.

C. Assessment

31. **Overall assessment.** The RFI provided expeditious access to a meaningful amount of funding (about 2 percent of GDP, one-third of the initially estimated external financing gap). Disbursement was delayed owing to disagreement between the government entities on the division of funds, but this was a matter out of staff's hands. While the RFI helped the country during 2020, the economic effects of the pandemic were relatively long-lasting (particularly since the second and third waves of infection lasted well into 2021). Based on staff's medium-term projections in February 2021, the output gap is expected to remain substantially negative through 2024 and the current account considerably weaker than pre-pandemic through 2025.

32. **Differences in approach to conditionality.** The grim outlook raises questions about whether the IMF could have taken an approach to the provision of financing that would have left the country in better shape over the medium run while still meeting critical needs during the first year of the pandemic. The RFI was provided without prior actions and, by the nature of the instrument, with no ex post conditionality. Though some staff recommendations, mainly for financial sector reforms, were included in the LOI and ultimately implemented, staff saw these as minor relative to the range of structural reforms needed for boosting investment and employment creation. The World Bank and EU made also significant financing commitments by mid-2020 but, in contrast to the Fund, disbursements were delayed, first because BiH authorities took several months to ratify the legislation associated with these loans and then because of the absence of progress on policies. This appears to reflect a difference of approach between the IMF on the one hand and the World Bank and EU on the other. While all three institutions agreed on the nature and need for the reforms for the medium run, the Bank and the EU maintained some priority on structural reforms, while the Fund set aside this consideration to meet the immediate needs of the pandemic. The Fund's strategy was premised on a follow-up UCT arrangement under which medium-run issues would be tackled, but no progress on this had occurred as of end-2021.

33. **Governance safeguards.** The IMF came under significant criticism from the domestic press and civil society because of the perceived inadequacy of the mechanisms for transparency in the use of RFI funds. Though emphasis on such safeguards and monitoring of their implementation strengthened over time, the provision of the RFI under initially lax safeguards may nevertheless have negatively impacted public perception of the IMF.

34. **Staff analysis and projections.** The actual drop in activity in 2020 was somewhat smaller than projected. Broadly, a larger-than-expected collapse of private demand was offset by much higher government spending (reflecting the execution of government investments long-in-the-planning stage but unrelated to the pandemic) and a much stronger recovery in the external balance. Although total external financing proved to be somewhat less than expected, the current account deficit substantially undershot projections, owing to weaker-than-expected imports and much stronger remittance and tourism receipts. The central bank was therefore able to increase official reserves by €275 million instead of a drawdown of €100 million as projected.

IV. Kosovo

35. **Overview.** Expecting a sharp hit from falling tourism receipts, remittance inflows, and domestic containment measures, staff projected a large drop in GDP in 2020, with a commensurate increase in the fiscal and current account deficits. Nevertheless, Kosovo received Fund support through an RFI of only 50 percent of quota—reflecting concerns about political instability that caused Fund staff to take a cautious approach to financing. Moreover, staff were strongly of the view that a UCT program was needed, though this was not stated as a consideration in going ahead with a request for only 50 percent of quota. With a strong recovery in 2021 eliminating a BOP need, the authorities were advised not to seek the remaining 50 percent of quota under the RFI. Despite expressed interest in a UCT arrangement in the Letter of Intent (LOI), program negotiations broke down in early 2021 when the government changed again and have not resumed.

A. Background and Economic Developments

36. **Initial conditions.** Pre-pandemic, the Fund estimated potential GDP growth at 4 percent. Given that Kosovo uses the euro as its currency, inflation was expected to remain low. An effective fiscal rule constrained current deficits to less than 2 percent of GDP; public investment added to that modestly. The banking system had comfortable capital and liquidity buffers and low non-performing loans, although staff saw pockets of risk developing. Current account deficits ran large but were amply financed by FDI and other inflows. Public and external debt ratios, each at about 20 percent of GDP, were expected to rise slowly: sustainability was not a problem. International reserves were low by regional standards, but surpassed Fund metrics for adequacy.

37. **Pre-pandemic advice.** Staff advice centered on broad-based structural reforms that were urgently needed to raise growth potential: strengthening governance, raising fiscal revenue, increasing labor force participation, improving competitiveness, and raising infrastructure spending. For the previous two years, however, successive changes in government and emerging populist pressures had stalled reforms.

38. **Impact of COVID-19.** An expected hard drop in tourism receipts and remittances together with falling domestic demand in the face of COVID containment measures fed into a projected drop in GDP of 5 percent in 2020 (Table 2). The brunt of the drop was expected to be concentrated in the middle of the year, after which a reasonably strong, but partial, recovery was projected for the rest of 2020. Inflation was expected to remain low. Fiscal revenues were expected to drop by 12 percent in 2020 owing to both lower activity and tax relief for companies and individuals. Pandemic support measures were covered by reallocations from other spending categories, while the overall spending envelope was cut. Still, a significant deviation from the fiscal rule (broadly, limiting the current fiscal deficit to no more than 2 percent of GDP) was considered inevitable. The external position was expected to come under serious strain. While the deficit on goods and services account was expected to narrow slightly, primary and secondary income surpluses were expected to fall significantly.

Table 2. Kosovo: Selected Economic Indicators

	2019	2020				2021
	Actual[3]	Projections pre-COVID[1]	Projections COVID[2]	June WEO	Actual[3]	Actual[3]
GDP growth (Percent)	4.8	4.0	-5.0	-6.5	-5.3	9.5
Inflation (Percent)	2.7	1.5	1.3	1.1	0.2	3.3
Budget balance (Percent of GDP)	-2.9	-3.7	-4.8	-8.1	-7.9	-1.6
Government debt (Percent of GDP)	17.7	20.5	20.7	23.5	22.5	22.5
Current account balance (Percent of GDP)	-5.7	-6.6	-7.4	-8.4	-7.0	-9.1
Official reserves (Billions of €)[4]	0.8	0.8	0.7	0.7	0.7	0.9

Sources: IMF; IEO staff calculations.
[1] January 2020 WEO (IMF, 2020c); [2] Staff Report of Request for RFI (IMF, 2020d); [3] July 2022 IMF WEO;
[4] Numbers from WEO were converted using end-period exchange rate.

39. **Nonpharmaceutical interventions.** The government instituted a lockdown, travel restrictions and other containment measures promptly. These policies proved highly successful in limiting infection rates in the first wave. But as measures were eased in mid-2020, the second wave was severe, so containment measures were reinstated with rather quick success. The third wave, starting at end-2020, was yet more severe and stretched the capacity of the healthcare system but did not dent economic activity and foreign exchange inflows as much as the first two waves. By mid-2021, the economy was recovering strongly.

40. **Fiscal response.** Implementation of fiscal support measures agreed by a caretaker government with staff in April 2020 were delayed until June when a Parliamentary coalition was formed. Once approved, the measures were implemented broadly as envisaged in the RFI letter of intent. Spending was redirected to sensible pandemic relief objectives: allocations to the health system to cover costs of personal protective equipment (PPE), vaccines, and wage supplements for healthcare and other essential workers; financial transfers to beneficiaries of social and pension schemes, with extra amounts directed to the poorest households; tax relief to firms mainly in the form of delays in tax payment deadlines; encouragement to firms to retain employees by briefly suspending employers' pension contribution and by extending salary subsidies for certain types of employment, and steps to ease the burden on firms from repaying bank loans. Demand stimulus took the form primarily of allowing early tax-free withdrawals of up to 10 percent of individuals' pension accounts, just over half of which the government would reconstitute gradually beginning in 2023 from public funds. Publicly owned enterprises also received budgetary support.

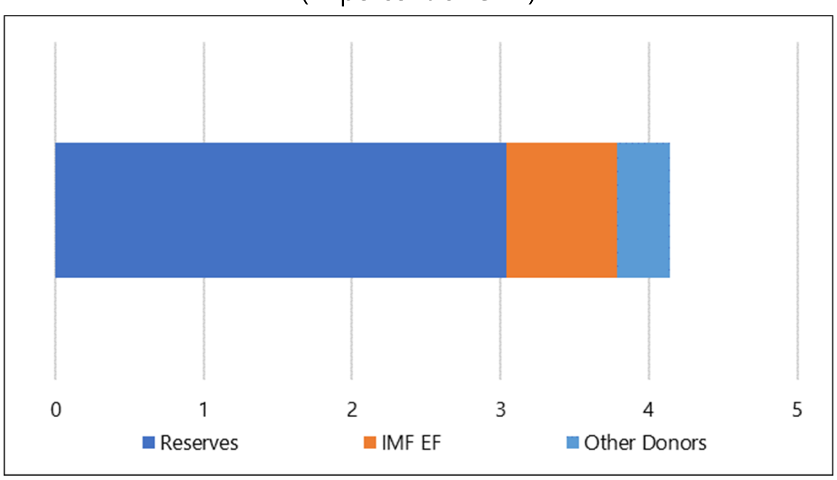
B. Engagement with the Fund

41. **Access level.** Financing was initially expected to be very tight. Just before the staff visit to discuss the RFI at the end of March 2020, another in a series of no-confidence votes since 2019 led to the installation of a caretaker government, operating without Parliament. Although this government was functional, staff were concerned about a return of the political uncertainty of the

previous two years vis-à-vis the conduct of policies. Thus, the RFI was for only 50 percent of quota for Kosovo, in contrast to most other EUR countries whose agreements on RFI purchases were also negotiated before the Board's mid-April decision to raise the access limit on RFIs to 100 percent of quota but whose requests were adjusted to obtain 100 percent of quota in financing. Staff indicated to Management and in the Board discussion to approve the RFI that the remaining 50 percent would be disbursed as soon as a government was in place and provided that the pandemic emergency continued to impact the normal functioning of government. While justified by the absence of a permanent government, this decision to limit access to 50 percent of quota was described by some staff as inconsistent with the approach chosen for other EUR countries.

42. **International reserves and reliance on domestic financing.** Large domestic financing was assumed as the RFI request went to the Board in April 2020. The external financing gap was estimated at €284 million (about a 4.1 percent of GDP and a quarter of 2019 gross international reserve holdings)—see Figure 5. Of that projected external financing need, only €76 million was expected to be filled through the RFI and limited amounts of identified financing from the WB and the EU. The lack of identified external financing sources meant that a sharp reduction in international reserves (around €209 or 3 percent of GDP) would be needed. External debt (predominantly to the International Development Association, EIB, EBRD, and IMF) relative to GDP was expected to be stable at about 20 percent of GDP. Similarly, of the projected total fiscal financing need of €606 million (around 9 percent of GDP), only €105 million (or around 1.5 percent of GDP) was expected to be filled through the RFI and identified IFI funding. This implied that large domestic financing—principally through drawdowns of government deposits at banks—would be necessary. Staff expressed concern about implications for both bank liquidity and the adequacy of the remaining fiscal buffer. Although public debt was projected to rise rather sharply, it would remain sustainable in the staff's view. The lynchpin in these calculations was that the fiscal rule would be reinstated in 2022 and that GDP would recover, which was in fact the case.

Figure 5. Kosovo's Ex Ante Balance of Payments Gap
(In percent of GDP)



Sources: Staff Report (IMF, 2020d); IEO staff calculations.

43. **Governance safeguards.** Kosovo's RFI was approved before the strategy on governance safeguards for emergency lending in the context of the COVID-19 pandemic was fully developed and did not include specific commitments in this area. Subsequently, most countries drawing on RFI/RCF made commitments (i) to publish procurement contract information, (ii) to collect and publish beneficial ownership of contractual parties, (iii) to prepare report on COVID-19-related spending, or (iv) to publish ex post audits of crisis-related spending. Headquarter instructed the Kosovo team to use the Article IV consultation in September 2020 "as an avenue to urge the authorities to adopt these commitments, not just in the context of the pandemic but more broadly." In practice, many of these measures had already been implemented in the government's six-month financial report for January–June 2020, which included a detailed report of COVID related spending. Moreover, provisions to make e-procurement mandatory for every project were being implemented. Further progress continued after 2020 with the publication of a special audit on COVID-related spending in August 2021, the preparation in 2022 of an additional audit report on the performance of COVID-related spending (IMF, 2022a, Annex V), and the execution of 100 percent of public procurement through e-procurement since early 2021.

C. Assessment

44. **Overall assessment.** The authorities were appreciative of the quick disbursement of the RFI. Despite a hard hit from the pandemic, Kosovo received an RFI of only 50 percent of quota. A second RFI disbursement might have been considered. The underlying decision to limit access had a reasonable basis in concerns about political stability, although it appears not to have been fully consistent with simultaneous decisions on other EUR countries, especially BiH, where similar concerns were also present.

45. **Influence on policies.** The government was in fact able to carry out appropriate short-term macroeconomic policies to address the risks of the pandemic, and external conditions proved far more benign than expected. Despite good progress in several areas including the use of e-procurement for 100 percent of budget purchases, the creation of commercial courts, and the reduction of informality, it remains unclear how transparent the fiscal support measures were. Moreover, even the limited progress with structural reform of the previous few years ground to a halt and in some areas might have been reversed. It would have been reasonable to nudge the authorities in the negotiations and in the staff report associated with the financing request to undertake some of the easier reforms that had been discussed earlier and had already benefited from some preparatory work.

46. **Staff analysis and projections.** The RFI negotiations took place at a time when the pandemic was still a new phenomenon and uncertainty was high. Discussions with the authorities were held weekly to monitor events and be ready to provide help as the situation evolved. Despite the uncertainty, the staff projection for GDP in 2020 was broadly accurate, but activity was supported by stronger-than-expected fiscal support and inflows from the diaspora. Private savings rose sharply. The management of mitigation measures kept severe health effects at bay until October 2020 when a very strong third wave stretched healthcare capacity. Nevertheless, the most serious economic

effects occurred in the first two quarters of the pandemic. The ability to increase the fiscal deficit was due to the much larger availability of financing than had been secured at the time of the Board meeting, reflecting the fact that the IMF operated much faster than other stakeholders in the case of Kosovo. The current account deficit was somewhat smaller than projected reflecting a far weaker balance on goods, but far stronger diaspora tourism receipts and remittances/inward transfers (stronger, in fact, than in 2019).

47. **Catalytic role of the Fund.** In interviews, staff felt that the April EF had helped catalyze the availability of other sources of external funding, although this is a rare case among our case studies for this evaluation where the authorities disagreed. What is clear is that the World Bank, the Council of Europe, and the EU as well as other IFIs (for example, the EBRD) provided substantially more external financing than initially anticipated in April 2020, so that the use of reserves was much less than projected. While the decision to expand the list of IMF eligible instruments to unlock funds under the EU's MFA was not made in a vacuum given the coordination that was taking place at the level of the G20 and regular contacts between the European Commission with IMF country teams, it was neither "encouraged nor discouraged" by the Fund according to interviews with EU officials. The first and second disbursements of the MFA occurred in October 2020 and in June 2021, respectively.

V. CONCLUSIONS

48. **Timely and well-appreciated help.** The Fund came to the aid of several low- and lower middle-income European countries at a time of critical need with timely financing instruments. While advanced economies in Europe did not have need for the IMF's financial resources, they benefitted from the positive experience of intensified and more cross-country surveillance efforts, mitigating the loss of individual consultations during the period of the temporary suspension of Article IV consultations.

49. **Reflections from case studies.** The case studies of two countries that received financing (BiH and Kosovo)—albeit at different access levels—and two countries that did not receive support (Belarus and San Marino) provide several reflections useful for calibrating the Fund's response during future crises:

- *Level of access and perceptions of evenhandedness:*
    - Kosovo's access was held at 50 percent of quota because of concerns about political stability, whereas BiH received 100 percent of quota despite political tensions between the entities of the country. While staff do not try to take sides in the internal politics of countries, the experience of the two countries illustrates that decisions on access levels do rest in part on staff's judgments on how political developments are likely to impact the choice of polices and hence impinge on the ability to repay the Fund. Viewed from the outside, this can feed perceptions of lack of evenhandedness in decisions about access.

  - While the two countries which did not receive Fund financing can also raise concerns about evenhandedness, it is not difficult to understand the staff's positions on why agreement on EF could not be reached. Nevertheless, both countries were in evident need and staff and the authorities agreed that Fund financing would have been helpful. In future crises, one could consider the possibility of having more tiered access in such very difficult cases, holding out possibility of further access with progress on policies.

- *Catalytic role and differences in approach:*

  - In the two cases where the Fund provided financing, the Fund's support was followed by additional financing, particularly from other official sector sources and remittances. However, in BiH, the World Bank and the EU delayed disbursements pending progress or understandings on policies, including some medium-run reforms. While the Fund's approach of providing timely support without conditionality was certainly highly valued, some consideration could be given in future crisis situations to whether it could be better to adapt a more tiered approach, with quick initial access followed by further access once policy conditions are met. The different approach followed by other institutions, and the views of some interviewed EUR staff, suggest that in at least in some cases, some degree of emphasis on conditionality can help countries' medium run prospects without jeopardizing immediate needs to mitigate the effects of the crisis.

  - In the two countries where the Fund did not provide financing, authorities saw this development as a negative signal to market participants. Both countries were, however, able to obtain additional financing from other official sources and from markets—albeit at more costly terms.

- *Governance safeguards*: These should be an essential part of the provision of EF in the future; laxity on this score can pose a reputational risk to the Fund.

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