

4

ASSESSING THE EFFECTIVENESS OF IMF ENGAGEMENT

HOW MUCH IMPACT HAS THE IMF HAD IN FRAGILE STATES?

The IMF's role in fragile states, compared to other member countries, has been particularly important in: (i) providing support in early stages of macroeconomic stabilization after a period of conflict or a natural disaster; (ii) providing a macroeconomic framework valuable for coordinating policies within a country as well as for facilitating engagement by international partners; and (iii) helping to build basic policymaking and institutional capacity in the core areas of IMF expertise. In the view of most stakeholders, the IMF has played its role quite effectively in these areas, though concerns remain that its impact may not have reached full potential.

Financing and signaling roles

The IMF's direct financing role was often limited in fragile states, compared to total DAC official development assistance (ODA) (Figure 7). This in part reflects the fact that the IMF is not the cheapest source of concessional financing. Even though the IMF can now lend interest-free from the PRGT, many fragile states have recourse to more concessional sources of donor money, including much longer-term loans and grants.²⁴ Moreover, the IMF's obligation to safeguard its resources has in some cases limited its willingness to increase exposure to fragile states, whose capacity to fulfill an agreed economic program and to service debt is uncertain.²⁵ In some countries (e.g., the Democratic Republic of the Congo, Liberia, Sierra Leone, Somalia) the need to clear IMF arrears before entering a new arrangement delayed IMF financial involvement, although the clearing of arrears was accelerated when there was strong international support to take advantage of an opportunity to cement political change (e.g., Democratic Republic of the Congo, Liberia).²⁶ On occasion, the IMF moved quickly to provide what was effectively grant support after a natural disaster (e.g., following the earthquake in Haiti and the Ebola crisis in West Africa).

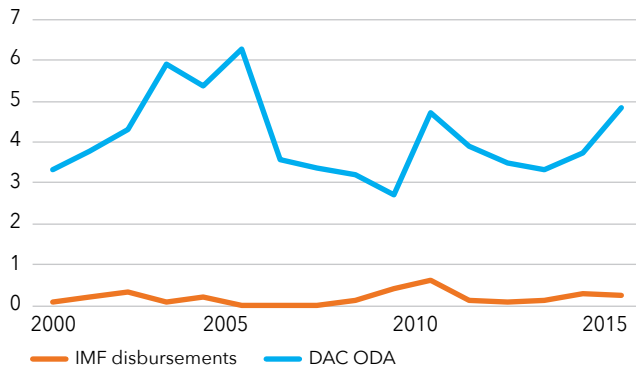
The IMF's main financing role in FCS has been catalytic. Stakeholders who were interviewed for this evaluation broadly agreed that the IMF had played a critical signaling role, providing the donor community with a degree of assurance that a country's public finances were benefiting from IMF guidance and monitoring and that donor financial assistance would be used in a transparent and sustainable macroeconomic framework. Development partners often considered IMF involvement in a country—especially in the context of a financing arrangement—as a *de facto*, if not *de jure*, precondition for their own financial engagement. Given this special role among a country's development partners, the IMF has typically exercised considerable influence with the authorities well beyond the amount of financing it provides, including in situations

²⁴ Currently, interest rates charged by the ECF and RCF under the PRGT are set at zero with a grace period of 5.5 years and a repayment period of up to 10 years. The SCF also carries a zero interest, but its grace and repayment periods are shorter at 4 and 8 years, respectively.

²⁵ As of November 2017, the average outstanding credit balance of 23 FCS borrowers was 20 percent of the access limit under the PRGT's UCT facilities.

²⁶ At present, only Somalia and Sudan remain in protracted arrears to the IMF. The Fund cannot lend to a member in arrears.

FIGURE 7. OFFICIAL FINANCIAL FLOWS TO FRAGILE STATES, 2000–15: IMF DISBURSEMENTS VS. TOTAL DAC ODA
(In percent of FCS GDP)



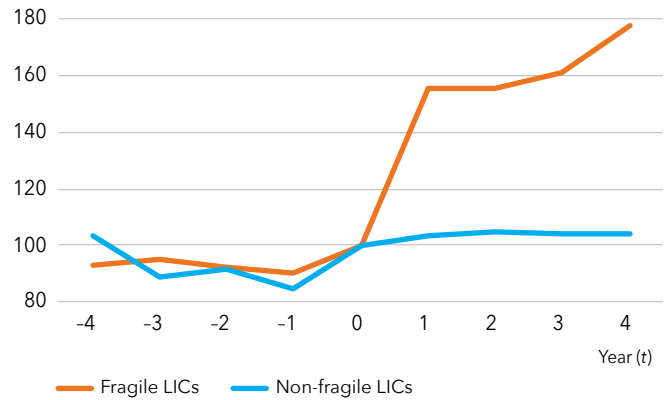
Source: IEO estimates based on IMF and OECD data.

where countries have preferred not to access IMF financing (e.g., Myanmar, Timor Leste).

The IEO’s analysis provides evidence for this catalytic role, showing that an IMF arrangement has typically been associated with a marked increase in donor support to FCS (Kuruc, 2018). Figure 8 depicts, for the period 2000–12, how the volume of total ODA flows to fragile and non-fragile LICs changed following the approval of an IMF arrangement, with or without financing (indicated by $t=0$, where the volume is indexed to 100). In the case of fragile states, the volume rose on average by 60 percent in the first year and remained at that level or higher for three additional years. In non-fragile LICs, no sharp pickup in ODA flows was observed. A similar strong catalytic role of an IMF arrangement was observed for fragile, but not for non-fragile, middle-income countries. While this does not prove that an IMF arrangement necessarily caused donor support to increase, it does suggest that the IMF plays a special coordinating role in the international community’s concerted effort to engage with fragile states.

It is difficult to establish conclusively whether IMF lending to a fragile state had a favorable, growth-enhancing effect, because it is not possible to isolate the impact of IMF intervention from the influence of many other factors, including the confidence effect of a ceasefire, in the case of a

FIGURE 8. THE IMF’S CATALYTIC ROLE IN FRAGILE VS. NON-FRAGILE LICs, 2000–12
(Average ODA Flows Surrounding Approval of IMF Arrangement (index=100 in year $t=0$))



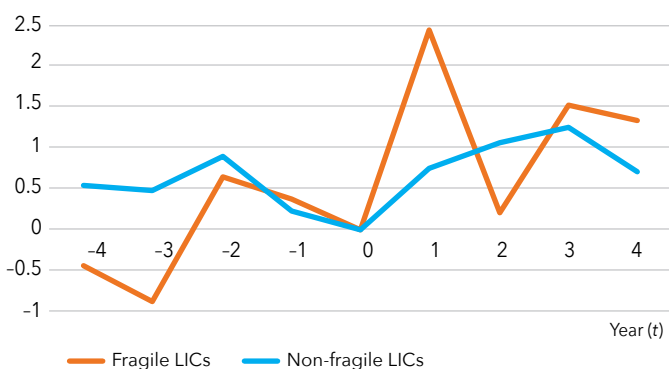
Note: Event-study methodology is used; includes both financing and non-financing arrangements; for details, see Kuruc (2018). Source: IEO estimates based on OECD data.

post-conflict state, or the financial and other contributions of development partners. Nevertheless, evidence does suggest that IMF lending has been associated with an upturn in economic growth in FCS: before/after comparisons of GDP growth during the period 2000–12 indicate that IMF financial support often began at a turning point from a period of decline or stagnation to a strong recovery (Figure 9). In non-FCS, the growth acceleration following IMF lending was much less marked. While causality is not established, these contrasting experiences may reflect the fact that fragile states often approached the IMF following a prolonged and economically damaging conflict, while non-fragile states came to the Fund when they faced a less deep cyclical setback (such as a commodity price downturn).

Many stakeholders noted that even where the IMF did not play a direct financing role, it could still strongly influence FCS outcomes by establishing a framework for macroeconomic stabilization. This could (though did not always) occur through a Staff-Monitored Program (SMP) designed to provide a track record of policy performance that international partners could use as a basis for providing financing (e.g., Myanmar, Somalia). However, interviewees thought that SMPs provided a less effective signal than programs qualifying for UCT conditionality, where the IMF had “skin in the game.” In some countries, the authorities relied heavily on the IMF staff for preparing a macroeconomic framework, including

FIGURE 9. REAL GDP GROWTH IN FRAGILE VS. NON-FRAGILE LICs, 2000–12

(Percentage difference relative to the year ($t=0$) of IMF arrangement approval)



Note: Event-study methodology is used; includes only financing arrangements; for details, see Kuruc (2018).

Source: IEO estimates of GDP growth based on data from Earth Observation Group, National Oceanic and Atmospheric Administration, and Penn World Tables.

preparing forecasts and even formulating a budget; IMF surveillance also provided a set of consistent fiscal and other macroeconomic data for the donor community. Most of those interviewed emphasized that no other institution had the capacity to play this role.

Country officials stressed that in an environment where either the government is fragmented (as in Bosnia and Herzegovina) or its administrative capacity is weak, the IMF often provided a valuable vehicle for interagency coordination. For instance, when a country comes to agreement on a program or completes a program review with the IMF, different branches of the government are compelled to coordinate with each other in terms of budgetary or policy commitments. In those few FCS that had some access to market financing or were attempting to attract foreign direct investment (e.g., Angola, Côte d'Ivoire), the IMF's assessment of the soundness of their economic policies or their medium-term economic outlook played an important signaling role. A number of officials interviewed cared deeply about what IMF staff reports said about their countries, irrespective of whether IMF financing was being sought.

Capacity development role

Country officials stressed that capacity development was the area where the IMF could make its greatest contribution. Many observed that the IMF had played a crucial role in building capacity at the central bank and the ministry of finance, particularly when countries emerged from periods of civil conflict (e.g., introducing new currencies, basic central banking operations, or a budgetary execution and monitoring framework in Afghanistan, Bosnia and Herzegovina, Cambodia, the Democratic Republic of the Congo, Iraq, Liberia, Rwanda, and Timor-Leste). Likewise, most interviewees valued the role the IMF could play as an external advocate in supporting the reformers against stiff domestic political opposition, in such areas as revenue mobilization and banking supervision. At the same time, interviewees generally acknowledged that long-term progress beyond an initial phase could be slow and subject to setbacks, particularly in countries with weak institutional capacity and governance.

Role in governance issues

Officials and experts expressed a range of views on how much the IMF should be involved in tackling governance-related issues. As noted in the previous chapter, many fragile states have deep-seated corruption and related governance problems. To the extent that these are at the root of fragility, many said that the IMF should be more heavily involved in promoting reforms to address them directly, especially in areas of its core competence such as public financial management and banking supervision.²⁷ By contrast, a few warned that aggressively addressing this area, especially at the outset of engagement, could undermine the political capital of authorities who were dependent upon support from all stakeholders. Some expressed concerns about the IMF's capacity to effectively address complex politically sensitive internal situations, and others were reluctant to see the IMF broadening inappropriately the scope of program conditionality.

More broadly, some experts observed that the IMF could only play a limited role in FCS, especially where endemic corruption presents enduring obstacles to reform and leads to aid fatigue, and where security concerns disrupt the continuity and quality of the policy dialogue. These experts argued that because, in their view, the IMF's mandate was not economic development, much less state building, it should wait until a

²⁷ The case study on Afghanistan (Chapter 1, Takagi and others, 2018b) documents how corruption played a role in the Kabul Bank crisis.

TABLE 4. IMF LENDING ARRANGEMENTS COMPLETION, 2010–17: FRAGILE VS. NON-FRAGILE STATES
(In percent of total)

	LOW-INCOME COUNTRIES		MIDDLE-INCOME COUNTRIES		ALL LOW- AND MIDDLE-INCOME COUNTRIES	
	Fragile	Non-fragile	Fragile	Non-fragile	Fragile	Non-fragile
Concluded	30	75	17	57	27	67
Not fully concluded	30	0	33	7	31	3
Cancelled	35	19	0	29	27	23
Off-track	0	6	17	7	4	3
Quickly off-track	5	0	33	0	12	3
Total	100	100	100	100	100	100

Note: All arrangements approved as of January 2010 and ended by end-December 2017, under the ECF, SCF, SBA, and ESF, but excluding undrawn precautionary arrangements and rapid disbursement facilities. “Concluded” means programs for which all scheduled reviews were completed; “off-track” those with no more than two reviews completed; and “quickly off-track” those with no or one review completed. Totals may not add up to 100 because of rounding.

Sources: IEO estimates based on SPR, Fund Arrangements since 1952; Monitoring of Fund Arrangements (MONA) database; IMF Members’ Financial Data by Country; country staff reports.

minimum level of security and capacity was established before it engaged with a country. In contrast, many other experts expressed the view that basic macroeconomic stability was a prerequisite for embarking on a path to economic development and state building; helping these countries achieve medium- and long-term macroeconomic stability, consistent with the Fund’s mandate, would in turn require the building of robust institutions. Therefore, in their view, the IMF must be present in a country, irrespective of the risks involved, as a precondition for the success of attempts to build resilience. Proponents of this view called for the Fund to have a comprehensive forward-looking strategy to engage with a fragile state, working closely with committed international partners.

On balance, this evaluation finds a compelling case for IMF engagement with governance issues from an early stage. However, engagement requires humility and patience, recognizing that there will be setbacks and disappointments. The IMF must also accept that most governance concerns that need to be tackled are in areas outside its core competence and therefore require close collaboration with the government and development partners.²⁸

HAVE THE IMF’S INSTRUMENTS BEEN ADEQUATE TO MEET THE NEEDS OF FRAGILE STATES?

The evaluation team examined whether the IMF’s arsenal of financing and non-financing instruments was adequate to deal with the challenges of post-conflict states. The overwhelming majority of IMF mission chiefs interviewed believed that the existing arsenal was adequate, and a similar view was expressed by 52 percent of the staff members responding to the IEO survey who had worked on fragile states (de Las Casas, 2018). IMF mission chiefs believed that, despite the relatively short-term orientation of IMF instruments, they had been able to adapt, as necessary, by employing different combinations of instruments successively (e.g., use of back-to-back programs) to help achieve desired longer-term objectives. Few of the country authorities interviewed questioned the adequacy of existing instruments, but rather focused most of their concern on the issues of access and conditionality.

To assess whether existing instruments had been tailored effectively to the needs of fragile states, the evaluation team

²⁸ See IMF (2017d) for a fuller discussion of the IMF’s approach to corruption and other governance-related issues.

TABLE 5. CONDITIONALITY IN FRAGILE VS. NON-FRAGILE STATE ARRANGEMENTS, 2006–17
(Average number of conditions per completed review)

TYPE OF CONDITIONS	2006–09		2010–13		2014–16		2017 (preliminary)	
	Fragile ¹	Non-fragile	Fragile ¹	Non-fragile	Fragile ¹	Non-fragile	Fragile ¹	Non-fragile
Low-income countries								
Total conditions	18.9	14.9	18.6	15.3	18.8	19.1	24.1	20.5
Of which: Performance criteria	7.9	7.1	7.9	6.7	8.0	6.2	11.2	8.0
Structural benchmarks ²	7.5	5.6	6.2	4.8	6.0	6.9	4.1	1.9
Others	3.5	2.2	4.5	3.8	4.8	6.0	8.8	10.6
Middle-income countries								
Total conditions	18.9	19.1	20.7	13.8	23.7	18.4	35.3	18.8
Of which: Performance criteria	10.9	0.2	10.9	7.0	11.7	6.8	10.0	7.7
Structural benchmarks ²	6.7	6.8	6.9	4.3	4.0	6.3	3.5	3.8
Others	1.3	12.1	2.9	2.5	8.0	5.3	21.8	7.3

Source: IEO estimates based on Monitoring of Fund Arrangements (MONA) database.

¹Fragile states are identified by the 2015 SPR list.

²Includes structural performance criteria through 2009.

compared lending arrangement completion rates and levels of conditionality in FCS and non-FCS programs. Over the period 2010–17, only 27 percent of the IMF lending arrangements with all fragile states were fully completed (30 percent of those with fragile LICs and 17 percent of those with fragile MICs) (Table 4). The completion rate for all non-fragile countries was much higher, at 67 percent (75 percent of the arrangements with non-fragile LICs and 57 percent of those with non-fragile MICs). Among fragile MICs, the share of programs that went off track quickly (after no or only one review) was 33 percent, whereas no program went off track quickly for non-fragile MICs.

What accounts for these differences in program completion rates? It is difficult to distinguish between two alternative explanations: (i) the IMF was prepared to take more risks up-front in approving arrangements for fragile states even though the chances for successful completion were lower; or (ii) the programs were not sufficiently tailored to the specific

circumstances of fragile states, such as limited implementation capacity, divisive politics, or security challenges.

Some insight into the issue of whether IMF-supported programs have been sufficiently tailored to the needs of fragile states may be gained by looking at the number of program conditions. By this metric, the conditionality applied to FCS was not particularly different from that applied to non-FCS. From 2006 to 2017, the number of conditions (including prior actions, quantitative performance criteria, structural performance criteria, and structural benchmarks) was generally higher for fragile than for non-fragile states (Table 5), and this tendency was observed even after 2010, following the Fund's 2009 decision to terminate the use of structural performance criteria in all IMF-supported programs. While the number of conditions does not necessarily capture the intensity of conditionality, this observation is nevertheless consistent with the complaints that were often expressed by the authorities interviewed, namely that the IMF's UCT conditionality was too

demanding and did not take adequate account of their countries' more limited implementation capacity.

Although the 2012 Staff Guidance Note suggests that setting fewer conditions would be appropriate in the context of UCT conditionality (e.g., “a well-tailored pace of macroeconomic adjustment;” and “a strictly prioritized, gradual agenda of key structural reforms”), the IEO detected tensions within the IMF staff concerning the right balance between the number of conditions and the willingness to grant waivers when conditions are not met. Many in review departments stated that they were open to the idea of setting fewer conditions, but they were less willing to allow waivers because doing so would undercut implementation incentives.²⁹ Some of them considered that by setting fewer conditions or being more prepared to provide waivers, the Fund could undermine the signaling role of programs involving UCT conditionality, with potential adverse consequences for non-FCS users of Fund resources. In this context, former senior IMF staff members, among others, noted that UCT conditionality was in fact quite capable of accommodating the circumstances of fragile states, while pointing to the importance of combining fewer conditions with strategic waivers.

Most area department staff members interviewed considered the existing instruments to be adequate in principle, although some expressed concern that they were pressed to include more conditions than needed by reviewers or that the policy on waivers was applied just as strictly for FCS as for non-FCS. Some stated that tailoring existing instruments to the realities of fragile states would not be equivalent to having instruments that were specifically tailored to the needs of fragile states. Given that program reviews are subject to the IMF's discretion, neither the borrower nor the donor community has the assurance that a country will maintain an uninterrupted IMF program engagement.

A number of staff members pointed to a gap between the low-conditionality emergency financing facilities (RCF/RFI) and the more stringent UCT-conditionality arrangements. This gap could be a problem, given fragile states' susceptibility to shocks and associated need for quick-disbursing support as well as the challenges these countries face to implement policies consistent with UCT conditionality. In the 2008 FCS work review, the IMF staff observed that, given the short-term focus of the available initial instruments (including SMPs), the transition to EFF/ECF arrangements was judged in some cases to have been “premature” (IMF, 2008a). This judgment became the basis for a staff proposal for a new arrangement dedicated to fragile states. The proposal was rejected by the Board,³⁰ but the IMF has since sought to enhance its rapid access/low conditionality facilities. However, while most drawings under the RCF were at the annual access limits, actual use of the RCF has been well below the cumulative limit.³¹ Use of an SMP in parallel with a drawing under the RCF has also been limited.

Officials' concerns about the IMF's existing instruments related to access and conditionality.³² Here, types of fragile states need to be distinguished. On the one hand, countries in early phases of post-conflict reconstruction have typically enjoyed considerable goodwill from the international community, and therefore the availability of financing has not usually been an immediate concern except in difficult arrears cases. On the other hand, countries in a prolonged state of fragility have viewed the IMF as one of the few available sources of concessional financing. Many officials from such countries noted that their borrowing needs were great, given the pressures to invest in health services, education, and infrastructure, as well as to meet pressing security and refugee needs. They would like to see access increased, even though they recognize that the IMF is not a primary source

²⁹ The review process, in which the successive drafts of a policy note or staff report are subjected to comment and scrutiny by various departments, ensures that IMF policies are uniformly applied across the institution and that quality is maintained regardless of who is originating the work. SPR plays a critical role in this process by clearing all documents for management approval.

³⁰ According to the Acting Chair's summing up of the Board discussion, while “many” directors saw merit in the proposal for a new arrangement (termed the “Economic Recovery Assistance Program”), designed to allow a medium-term, systematic, and graduated IMF engagement, “a number of other Directors questioned the need for a separate financial instrument for fragile states,” noting that “financing for development should be left to institutions with developmental mandates.” International Monetary Fund, BUFF/08/42, March 31, 2008.

³¹ As of November 2017, the average outstanding credit balance of ten FCS borrowers under the RCF was 22 percent of quota, compared to the cumulative access limit of 75 percent.

³² Since 2015, access under the RCF has normally been limited to 18.75 percent of quota annually and 75 percent of quota cumulatively, but the annual limit is increased to 37.5 percent for the exogenous shocks window and 60 percent for the large natural disaster window. Access under the RFI is limited to 37.5 percent of quota annually and 75 percent of quota cumulatively, while normal access under the ECF is 75 percent of quota annually and 225 percent of quota cumulatively. See IMF (2017e).

of development financing. And they noted the importance of flexibility in applying conditionality, particularly in the face of shocks that could generate pressing spending needs—including in the area of security—that could run against overall spending limits.

At the same time, both officials and staff interviewed recognized that greater access implies increased indebtedness on the part of FCS borrowers and could also mean greater credit risk for the Fund. IMF financing, even at concessional terms, increases a country's debt burden, which implies that the maturity of IMF financing may also need to be lengthened if a high level of concessionality is to be maintained. It is not obvious that any fragile state should be borrowing significantly more from any source when its ability to pay is uncertain and given the long process required to build resilience through institution building. Clearly, grants would be the ideal form of financial assistance to fragile LICs (IMF, 2015e), but the IMF has almost no capacity to provide them. Even its capacity to lend at zero interest under the PRGT is constrained by the limited availability of resources.

IEO interviews with staff, officials, and other stakeholders suggested several ways forward, including for the IMF to: (i) advocate that other donors provide increased grants to FCS; (ii) seek to mobilize grant resources for its own use;³³ (iii) introduce a dedicated facility for FCS that would lengthen the maturity of IMF financing and require less stringent conditionality; and (iv) find ways to increase access under the existing PRGT facilities, for example by raising annual access limits under the RCF,³⁴ or by allowing for a short UCT arrangement as a bridge to a possible ECF arrangement (e.g., by not requiring that a member achieve a sustainable macroeconomic position in two years or less, as currently required under the SCF).

The last option of adapting existing PRGT facilities would seem to be the most practicable, if not the best, and could be advanced in the context of the current quinquennial review of LIC facilities that is now underway. Interviews with representatives of donor governments suggest little support for the IMF providing grants to FCS, not viewing development financing as the Fund's role. The idea of a dedicated facility for FCS would quickly run into issues of how to determine

which countries would be eligible and how to raise resources for such a facility; uniformity of treatment would rule out using not only General Resources Account (GRA) but also PRGT resources without rewriting the terms of the Trust. Nevertheless, irrespective of the solution, special treatment for fragile states necessarily implies increased access to resources because, at a minimum, softer conditionality means a slower pace of adjustment and implementation of structural reforms and hence a need for longer-term financial engagement.

HOW EFFECTIVE HAS IMF CAPACITY DEVELOPMENT WORK BEEN IN FRAGILE STATES?

The IMF has rightly highlighted its capacity development work as the “front and center” of its engagement with FCS (IMF, 2015b), because weak institutions are at the root of fragility. The severe lack of capacity in many fragile states implies large potential gains from IMF technical assistance, including in the building of inclusive, effective institutions. At the same time, the lack of institutional capacity also means that the ability to absorb and implement TA is generally limited. There are wide variations across countries in national ownership, and hence in the authorities' willingness to implement TA recommendations, and in institutional continuity.

The effectiveness and impact of IMF TA depends crucially not just on the quantity of TA but also on other factors, including whether the advice pays sufficient attention to the political and institutional context, the manner in which TA is delivered, whether there is a sustained commitment from the country itself, and how well the Fund's TA is coordinated with that provided by development partners. Most interviewees felt that IMF TA was generally well tailored to country circumstances, although the Fund sometimes showed a tendency to provide “best practice advice” rather than advice suited to the country's institutional capacity, which could often be best obtained by learning from experience in similar countries in the region.

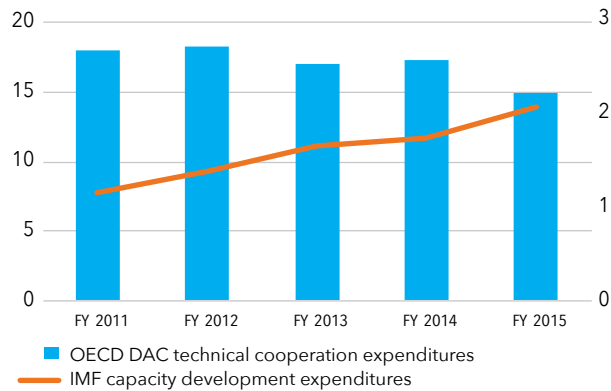
Coordination with partners is especially important because the IMF is a relatively minor player in the overall provision of TA to fragile states. While the IMF's share in the total

³³ One prominent external expert stressed the importance of tying the provision of grants to meeting conditions within the context of an IMF-supported program. To implement such a proposal, a trust fund would need to be established to allow the IMF to provide grants. Such trust funds were established following the Haitian earthquake and the Ebola crisis that affected three West African countries.

³⁴ Such an approach is consistent with the Staff Guidance Note, which encourages the use of the RCF as facilitating “sustained engagement, avoiding a ‘stop-and-go’ pattern that might result from targeting overambitious policies under a UCT arrangement.”

FIGURE 10. CAPACITY DEVELOPMENT EXPENDITURES ON FCS: OECD DAC TOTAL VS. IMF, FY 2011–15

(In billions of U.S. dollars—left scale; in percent of OECD DAC—right scale)



Note: Fragile states are identified by the 2015 SPR list.
Source: IEO estimates based on ICD data.

technical cooperation expenditures by OECD-DAC countries for fragile states has increased every year from FY 2011, it still made up only around 2 percent in FY 2015 (Figure 10). The IMF’s share is larger in the areas of its core competence, but even there the IMF must rely on other donors for implementation support (Kim, 2018b).

IMF TA in post-conflict states was particularly effective during the initial institution-building phase. Officials in almost every post-conflict state the IEO team interviewed had a highly positive view of the Fund’s early contribution to building capacity in areas such as revenue collection, public expenditure control, central banking, currency reform, and statistics (see, for example, the case studies on Afghanistan, Bosnia and Herzegovina, and Timor-Leste). In these areas, the IMF was uniquely qualified to support the design of core macroeconomic institutions when much of the capacity had been lost or destroyed during conflict (see Gupta and others, 2005, for a review of the IMF’s effort to help rebuild fiscal institutions in post-conflict countries).

Evidence is more mixed on the effectiveness of IMF TA when a country is in a prolonged state of fragility. A recent study prepared by the Fiscal Affairs Department finds some evidence of improved revenue and expenditure management performance in fragile states receiving IMF TA, but the

impact seems to have been quite small (IMF, 2017b). A senior official of a fragile state, explaining why the IMF’s TA work to raise the tax-to-GDP ratio in his country had had limited impact, highlighted the unwillingness of the public to provide resources to a government that was not perceived to serve their needs. In his view, IMF TA needed to be accompanied by measures to enhance the legitimacy of the state—an issue going well beyond the IMF’s expertise.

In interviews with the IEO, many senior country officials and IMF mission chiefs stated that, in their view, the IMF’s TA often tended to be better than that offered in similar areas by other donors. Consistent with this view, representatives of development partners pointed to the general strengths of central banks and of macroeconomic data—where the IMF has provided quite extensive technical assistance—compared to other types of institutions or areas of statistics, in many fragile states.

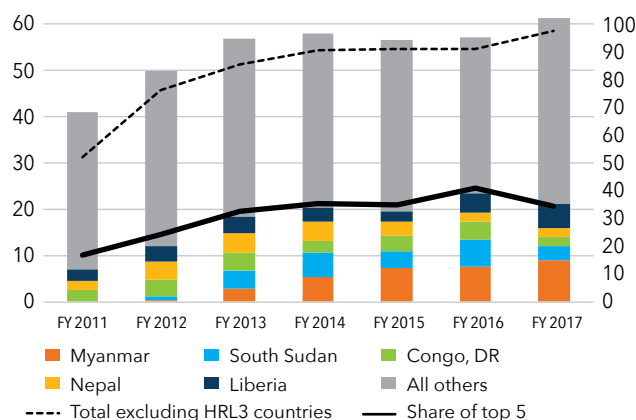
While judgements as to effectiveness varied, a clear message emerged from the interviews that the IMF’s TA delivery had improved in recent years. Many noted that the IMF’s general mode of operation in earlier years had typically been to send a team of technical experts to the field for a brief period, prepare a report outlining what was needed, and leave a copy with the authorities. This approach was particularly ineffective for fragile states. Often, especially in countries with severe capacity constraints, the report would sit in a desk drawer and little follow-up would take place. In more recent years, IMF TA has become more hands-on, with deployment of long-term resident experts and, increasingly, experts assigned from the Fund’s regional technical assistance centers (RTACs).³⁵ Most officials interviewed expressed a clear preference for resident experts as a source of easily accessed advice and support, while regional experts (though not a perfect substitute for “on-the-ground” assistance) were also seen as helpful in translating best-practice recommendations into specific country contexts.

Also showing improvement is the integration of TA with surveillance and program work. IMF country teams have made conscientious efforts in the past few years to integrate their policy advice in surveillance and program work with the technical assistance provided by functional departments. Some of these efforts are aided by the preparation of regional strategy

³⁵ At present, the IMF operates a network of 15 regional technical assistance centers located in the Africa, Asia-Pacific, Europe/Central Asia, Middle East, and Western Hemisphere regions. Their activities are funded by member and host countries, external development partners, and the IMF. See Kim (2018b).

FIGURE 11. IMF TA TO FRAGILE STATES, BY COUNTRY, FY 2011–17

(In person-years of field delivery—left scale; in percent of total—right scale)



Note: Fragile states are identified by the 2015 SPR list. The dotted line represents the volume of TA in person-years to all fragile states whose security risk rating by IMF Security Services was never HRL3, the highest risk category, at any time during 2014–16. TA delivered to multiple countries and regional institutions is excluded. Source: IEO estimates based on ICD data.

notes (RSNs) that have become routine, with the greatest value achieved by the specific country strategy notes that are now prepared for many countries. The African Department (AFR) is implementing a Capacity Building Framework on a pilot basis in four countries, mapping capacity development needs to TA delivery by functional departments and closely involving the authorities of the countries concerned, so as to motivate greater commitment. Likewise, the Asia Pacific Department has been preparing a three-year program for each fragile state to align surveillance with technical assistance, with the participation of TA departments and inputs from country authorities. More recently, the Middle East and Central Asia Department launched a similar initiative.

Nevertheless, there remains room for improvement in this area by applying best practice more consistently across departments. IEO analysis of a sample of staff reports for Article IV consultations with current and former fragile states reveals that TA-related issues were rarely discussed in the main body (except for a pro forma summary of recent TA missions), so the reports yielded little sense of TA impact or the views of TA departments, much less the IMF’s capacity development strategy. This omission limited the role concerned Executive Directors could play, for instance in facilitating coordination with bilateral TA providers. AFR has shown an encouraging way forward. Going beyond the pilots under the Capacity

Building Framework, the department is now requiring all country reports to include a dedicated section on capacity development activities in the main body and an appendix summarizing the country strategy.

Senior fragile state officials and aid experts expressed ongoing concerns about whether IMF TA was reaching its full potential. For example, in countries where implementation capacity is lacking, there is a large unmet demand for resident technical advisors—a finding that echoes previous IMF staff reviews (e.g., IMF, 2015c) and the view of 64 percent of the IEO staff survey respondents (de Las Casas, 2018). Another concern is that high security risk countries receive far less TA support on the ground, given constraints on staff travel, even though they may continue to receive support from IMF staff in neighboring countries. The authorities regarded out-of-the-country capacity development activities as much less effective and even potentially counterproductive: distance limited the number of officials who could be involved, thereby limiting the support received by officials as a team, while taking key officials out of the country for a period of time was seen as highly disruptive to the day-to-day functioning of a government.

Notwithstanding the Fund’s stated priority given to fragile states and a buildup in TA over FY 2011–13, IMF TA to such countries as a group has plateaued in recent years (see Figure 5). Moreover, it has been concentrated in a handful of countries. In FY 2017, for example, the top five recipients accounted for 35 percent of all IMF TA given to FCS in terms of person-years of field delivery (Figure 11). Myanmar and South Sudan have been particularly large recent recipients, though with very different experiences (Box 2). The IMF’s 2016 internal Risk Report, after noting the concentration of TA in a few countries, remarked: “Inflexibilities in internal prioritization processes, including the management of the resource allocation process and the competing demand and deployment of TA staff relative to donor funded projects, may be constraining responsiveness (IMF, 2016b).”

In understanding these trends, it is relevant to appreciate the role of demand versus supply in the allocation of TA resources in the IMF. In principle, all TA is demand-driven, given the requirement that support be requested by the government concerned. As the costs are not charged to the recipients, few governments have refused to accept free TA and most have usually been happy to receive more. But because the IMF’s TA resources are limited, supply factors play a critical role (Kim, 2018b). A careful internal

BOX 2. MYANMAR AND SOUTH SUDAN: CONTRASTING EXPERIENCE WITH IMF TA

Myanmar and South Sudan have been the two largest recipients of IMF TA in recent years, accounting for about 10 and 8 percent, respectively, of all TA provided to fragile states between FY 2013 and FY 2016. When they engaged with the international community, both countries faced enormous needs to build state capacity, the first as a nation emerging from decades of isolation and the second as a newly independent nation. When the IMF intensified its engagement with these countries in 2012, it placed capacity development at the center of its work, heavily funded by external donors and closely coordinated with development partners. The program of technical assistance, in both cases, was anchored within the framework of a Staff-Monitored Program.

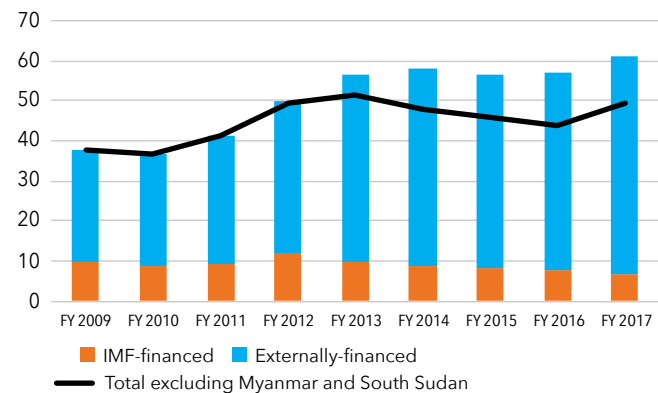
In Myanmar, the overriding objective of IMF TA was to help the country's transition to a market economy, focusing on building fiscal and monetary institutions, including the improvement of public financial management systems and the adoption of a floating exchange rate regime, and macroeconomic statistics. In South Sudan, a unique feature of the IMF's technical assistance program was the establishment of a Trust Fund for Capacity Building in South Sudan, to which the European Union, Norway, and the United Kingdom contributed. The large-scale three-year program, coordinated with the World Bank, the African Development Bank, the United States, and other TA providers, sought to build capacity in central banking, macroeconomic analysis and statistics, tax administration, and public financial management, including the management of oil revenue.

Outcomes could not be more different between the two countries. Myanmar has entered a phase of strong economic growth amid relative political stability (despite lingering ethnic tension), allowing the country to absorb TA and continue to develop human and institutional capacity. In contrast, South Sudan experienced the breakout of a civil war in December 2013. Missions to the country were suspended during a good portion of 2014 and, after a resumption in October 2014, have been suspended again since June 2016, with only limited work taking place outside the country. Recognizing the lack of absorptive capacity and in view of the security situation, the Trust Fund's steering committee agreed in 2015 to a scaling down of TA activities in South Sudan. The volume of TA to South Sudan declined sharply (by nearly three person-years) in FY 2017.

process is followed to determine the allocation of resources, taking into account the assessment of country needs and the effectiveness of TA work. On occasion, some TA has been proposed to the authorities on the basis of resource availability.³⁶

IMF staff members involved in TA administration and delivery emphasized the strong efforts that had been made to build up TA to fragile states, and suggested that the recent plateauing of TA provided to FCS mainly reflected concerns about the low absorptive capacity of fragile states, as reflected in a lack of progress in implementing TA recommendations, set against competing priorities.³⁷ Under these circumstances, they added, the apparent plateauing only suggests that the volume of TA to fragile states has reached roughly the capacity limit. A tightening of the travel rules that followed the tragic killing of an IMF resident representative in Afghanistan in 2014 was also highlighted, although the volume of TA has not

FIGURE 12. IMF TA TO FRAGILE STATES, BY FUNDING SOURCE, FY 2009–17
(In person-years of field delivery)



Note: Fragile states are identified by the 2015 SPR list; TA delivered to multiple countries and regional institutions is excluded. Source: IEO estimates based on ICD data.

³⁶ The IEO learned from various interviewees about cases in which multiple TA missions had visited a country towards the end of an IMF fiscal year, overwhelming the capacity of the country to receive them. As another example, a sophisticated financial sector mission was suggested to a country where there was no financial sector to speak of.

³⁷ For example, analytical support to the Group of Twenty is provided as technical assistance.

BOX 3. EXTERNAL EVALUATIONS OF DONOR-FINANCED TA ACTIVITIES

External evaluations have been conducted for the activities of RTACs, TA activities financed by multi-donor topical trust funds, and TA projects financed by some bilateral donors. The IEO reviewed twelve of these reports.¹ They vary widely in quality and do not generally address the issues of effectiveness or impact directly. Given their donor-mandated nature, their focus appears to be more on accountability than on learning.

The IEO's analysis identified the following issues as recurring challenges to the effectiveness of IMF TA in LICs and lower MICs, including some fragile states:

- ▶ Limited access of resident experts to policymakers;
- ▶ Limited coordination among TA providers;
- ▶ Lack of absorptive capacity;
- ▶ Lack of follow-up;
- ▶ Difficulty of recruiting qualified regional experts;
- ▶ Frequent change of government and reversal of reforms;
- ▶ High turnover of officials who leave civil service for higher paying jobs;
- ▶ Corruption and lack of commitment to reforms;
- ▶ Low national ownership.

For fragile states,² CLIC (2015) additionally highlighted the need to:

- ▶ Be on the ground even in difficult security environments to coordinate with partners;
- ▶ Combine technical support with organizational development to ensure sustainability.

¹ Murray and others (2009); Murray, Abrams, and Vaai (2009); Jones and others (2009); Global Partnerships (2011); Chatterji and others (2013); Woodbridge and others (2013); Certan and others (2014); CLIC (2015); Consulting Base (2015, 2016); DevTech Systems (2015); Watson and others (2015).

² This evaluation covered public financial management, tax administration, and financial sector reforms in six fragile states: Afghanistan, Iraq, Libya, Sudan, West Bank and Gaza, and Yemen.

increased much even for those fragile states where security risk was less of a concern (see the dotted line in Figure 11).³⁸

The IMF has relied heavily on external funding for TA to FCS in view of a binding internal budget constraint. As much as 75–89 percent of IMF TA to fragile states has been externally funded in recent years (Figure 12). Reliance on external funding could potentially limit the flexibility of IMF TA delivery, to

the extent that external funding is often earmarked for certain purposes. For example, when external funds are administered through country-specific trust funds (as in Somalia and South Sudan), the manner of TA delivery is strictly prescribed; if the security situation prevents TA being delivered to the designated country, the funds remain unused.³⁹ As a matter of practice, moreover, the IMF has sought to limit the overall TA budget in order to maintain the quality of its TA. As the IMF does not

³⁸ It is instructive in this context to note that the volume of TA to South Sudan remained significant despite the suspension of mission travel to that country (the IMF security risk rating for South Sudan was HRL2). See Table 7.

³⁹ IMF staff does not share the view that the lack of flexibility in external funding has adversely affected the volume of TA to fragile states. Rather, rising external funding has allowed total TA volume to expand in the environment of a tightening internal budget constraint.

outsource the delivery of TA to third parties, the limited ability to hire backstop staff potentially could also place an additional constraint on the amount of TA it can deliver (Kim, 2018b).

Is there solid evidence that TA to countries in a prolonged state of fragility is less effective than TA to non-fragile states? Although a systematic attempt by the IMF staff to assess the impact of IMF TA is just getting underway (e.g., IMF, 2017c), some information is available from periodic external evaluations of donor-funded TA projects prepared by private consultants (Box 3, p. 25). Two of these evaluations assessed the effectiveness of IMF TA in FCS and non-FCS during 2011–14 and yielded mixed assessments (Consulting Base, 2015; DevTech Systems, 2015).⁴⁰ The lack of strong evidence may mean that FCS and non-FCS at comparable stages of development face similar obstacles to IMF TA-driven structural reforms.

With the just-launched results-based management (RBM) framework for technical assistance, which is designed to “monitor the actual outcomes that the Fund hopes member countries will achieve” with the use of objective indicators and a rating system (IMF, 2017a), it is expected that impact assessment will become a routine part of IMF capacity development work.

However, some stakeholders expressed concerns that the otherwise welcome emphasis on accountability could potentially work against the interests of fragile states where weak implementation capacity militates against achieving quick impact. A decision by the IMF to pull out in the face of setbacks must be carefully weighed in a strategic context, preferably in consultation with development partners. Some senior country officials said that the recent increase in emphasis on accountability had made them reluctant to request TA from the IMF, because they were unsure of their ability to produce results within a short period of time; they had often been irritated by IMF staff repeatedly asking them about the impact of IMF TA, which in their view could only be assessed over the medium term. Thus, it is important to be realistic in the application of RBM to fragile states, so that achievable goals are set with an appropriate time horizon.

HAS THE IMF’S ENGAGEMENT BEEN SUFFICIENTLY TAILORED TO COUNTRY-SPECIFIC CIRCUMSTANCES?

The need to tailor policy advice or conditionality to country circumstances, important for any country, assumes even greater importance for fragile states. This is well recognized within the IMF. In 2015, the IMF committed to providing “more tailored policy advice that is sufficiently attuned to the political economy circumstances and flexible to adapting to the realities on the ground” and to enhancing its “policy analysis and advice to address the challenges of fragile states” (IMF, 2015f). Implicit in the need for political economy analysis is the recognition that, while weak governance and corruption are the key elements of fragility that need to be tackled, it is a complex matter to determine the appropriate pace and sequence of reforms in a specific country context.

The evaluation team sought to identify recurring issues or patterns in the IMF’s surveillance or conditionality that might deserve attention. Views differed widely even among officials and experts within the same country as to what constituted the best approach under a given circumstance. In general, incumbent officials tended to argue that the IMF should be “more realistic” in policy advice or “softer” on conditionality, while many former officials or those in the opposition typically supported a tougher IMF stance. Opinions also varied among donors on the ground and representatives of civil society. Some interviewees called for the IMF to be more understanding of local conditions, while others suggested that the IMF had been too “soft” on structural conditionality, especially when governance issues were involved, and that it had missed opportunities to apply its substantial leverage with the authorities.

Among the most frequently discussed policy issues was how to reduce costly fuel subsidies. In almost all the country cases reviewed for this evaluation, this issue arose in the context of engagement with the IMF. Many incumbent officials indicated that the IMF had pushed them too hard, not recognizing the political and social implications of lifting subsidies on fuels, but other informed observers said that the authorities’ arguments were largely self-serving. On occasions, a rapid pace of reform backfired even if it may

⁴⁰ Consulting Base (2015), rating the “overall effectiveness” of IMF TA in tax policy and administration on a scale of 1–4, gave average scores of 2.5 for 5 countries classified by the World Bank as fragile at any time during 2011–14 and 3.4 for 3 countries never classified as such during the same period. DevTech Systems (2015), likewise rating the “overall performance” of IMF TA on managing natural resource wealth on a scale of 1–7, gave average scores of 4.7 for 6 countries classified by the World Bank as fragile at any time during 2011–14 and 4.5 for 10 countries not classified as such during the same period. See Kim (2018b).

BOX 4. YEMEN: FUEL SUBSIDY REFORM

Fuel price increases in 2014 are sometimes seen as having precipitated Yemen's descent into civil war, and the IMF has been blamed for pushing too hard on subsidy reform without appreciating the risks. The story is more complex. The IMF's internal documents show that the staff had preferred a more gradual approach, coupled with a communications strategy to highlight the mitigating social spending measures being taken. But the government's more abrupt action in July 2014 was effectively forced by events.

The need for subsidy reform in Yemen had been well recognized for many years, and several attempts had already been made to tackle the issue, including in the ECF-supported program that was approved in 2010 (IMF, 2013a). In early 2014, the IMF sought to negotiate a new ECF-supported program that included a fiscal adjustment of 2.5–3.0 percent of GDP in 2014, coupled with a substantial reduction in fuel subsidies—which in 2013 accounted for about 7 percent of GDP, nearly 60 percent of the country's hydrocarbon revenue, and more than 20 percent of total public expenditures. The idea was to phase in the price increases gradually and use the fiscal space created from cutting the subsidies to increase quality investment spending and targeted social transfers.

Given the political and social sensitivity, the authorities remained reluctant as they negotiated a new program. However, the situation changed when attacks on oil facilities cut production, fuel shortages led to extensive black-market activity, and the decline in oil revenue put further pressure on the already deteriorating fiscal deficit. In July, the cash-strapped government raised fuel prices by a full 50 percent, with little indication of how social spending would be increased to protect the poor and vulnerable. The fuel price increase became a rallying point for the rebel movement to organize mass protests, which were a tipping point in the escalation of the Yemeni civil war (Ghobari, 2014; Robins-Early, 2015).

Even with the benefit of hindsight, it is difficult to know if there was a viable alternative. A former Yemeni official, an independent expert, and officials in the region stated that, given the unsettled political climate at the time, the subsidy reform should not have been attempted. But to maintain the existing level of subsidies (costing the government roughly \$10 million a day) would have required much more budgetary support than the donors were willing to provide. Given the precarious state of public finances, the fuel subsidies were clearly not sustainable. The rebel movement, after taking over the government in the capital city of Sanaa in 2015, totally removed the subsidies (Al-Shamahi, 2015). One informed commentary stated that the government should have done more to “develop political consensus around this reality” and to “prepare the public for the inevitable” (Greenfield and Milbert, 2014).

have been a sound course of action on technical grounds and difficult to avoid, as was the case in Yemen (Box 4).

Another recurring topic, particularly in the context of an IMF-supported program, concerned the limit typically placed on external borrowing. A number of officials complained that borrowing limits had been too tight in view of the enormous needs for investment in basic infrastructure such as roads, power plants, schools, and hospitals—investment that they saw as essential to accelerate growth and promote social spending and hence to underpin lasting economic (and political) stabilization. Clearly, there are difficult trade-offs. Debt sustainability is an important consideration, given that many fragile states have received debt relief under the Heavily-Indebted Poor Countries

(HIPC) Initiative (see Appendix 1).⁴¹ IMF staff has developed various analytical tools to assess the growth, fiscal, and debt sustainability impacts of investment strategies (e.g., Buffie and others, 2012; Melina and others, 2014; IMF, 2015e; 2015f). Country teams have used these and other analytical tools for a number of countries in recent years, but such analysis has informed practical policy advice in the context of the Article IV process only in a handful of fragile states (e.g., Chad, 2013; Liberia, 2012; Myanmar, 2014; Timor-Leste, 2017; Togo, 2011).

The above topics illustrate the perceived tensions that can arise between development and macroeconomic stabilization objectives as well as the heightened role of socio-political factors in fragile states. Other such topics were: (i) the

⁴¹ The HIPC Initiative, launched in 1996 by the IMF and the World Bank, involves two steps for countries seeking debt relief: (i) meeting certain conditions to become eligible (Decision Point) and (ii) showing progress under the agreed framework, including an IMF-supported program (Completion Point). For details, see <http://www.imf.org/en/About/Factsheets/Sheets/2016/08/01/16/11/Debt-Relief-Under-the-Heavily-Indebted-Poor-Countries-Initiative>.

appropriate build-up of official foreign exchange reserves (e.g., the Democratic Republic of the Congo, Liberia), with implications for exchange rate management and hence the domestic prices of key sensitive commodities; and (ii) involvement by the central bank in lending schemes to the private sector, as in Liberia, where the IMF staff objected to such a scheme on the grounds, inter alia, of the risks involved, but the central bank staff argued that, in a fragile state like theirs, what might be viewed as “unorthodox” monetary policy measures were required to address a shortage of funding available through conventional channels.

The 2011 staff review of IMF work on FCS concluded that “the forms of engagement [might] not have sufficiently taken into account the specific characteristics of fragile situations” (IMF, 2011a). This evaluation’s finding is that the evidence is mixed and inconclusive. For example, several case studies, including Chad and Côte d’Ivoire, found that the issue of corruption was candidly discussed in internal documents and staff reports. For Chad, the issue of military spending was extensively discussed by the staff from 2006, when the country’s oil resources began to flow.⁴² For Côte d’Ivoire, the 2011 Article IV consultation noted the positive role of the armed and paramilitary forces in combating smuggling, fraud, and border insecurity, and thereby boosting economic recovery. But these discussions of security spending were atypical of the IMF’s policy dialogue with FCS authorities, and in several cases corruption was hardly mentioned (see also IMF, 2017d for a similar finding). It is difficult to determine whether the difference reflected uneven attention to similar problems of critical importance, or the different degrees of importance of corruption or military spending in different countries.

Area department staff members interviewed observed that their efforts to incorporate greater country specificity in their policy advice or conditionality were occasionally undermined by the Fund’s interdepartmental review process. In their view, the process imposed too much uniformity (e.g., in terms of data requirements, analysis, topic coverage, or even table format)

where more differentiated treatment would have been warranted. Others complained that the review process gave too much weight to the consistency of numbers, and not enough to the quality of policies being discussed. Some more junior staff members felt that they would be risking their professional reputation if their policy advice or prescriptions were perceived as “too weak,” given the culture of the institution where, in the case of a program, the ability to negotiate tough conditionality measures is prized. Similarly, when asked by the IEO staff survey why the principles advocated in the Staff Guidance Note had not been applied in specific instances, 39 percent of respondents attributed the failure to an “IMF culture that places value on best international practice,” while 61 percent of them attributed it to “pressure from review departments.” Staff often perceived SPR reviewers as not understanding the specific circumstances of the country. In turn, the reviewers sometimes considered mission chiefs “too accommodating” on the pace and scope of reforms and often failing to make a sufficient case for differentiated treatment based on a well-grounded explanation of the sources of fragility.⁴³ There is no way of knowing which side was right in any given circumstance without fully investigating the specific merits of each position.

As a general proposition, some staff members suggested to the IEO that a possible key to resolving such conflicts between country teams and review departments would be to follow more rigorously and uniformly the injunction in the Staff Guidance Note stipulating that policy notes “should explicitly address the nature of fragility, including... political and social context” and should include “a brief discussion of the overall strategy that would help the country transition out of fragility” (IMF, 2012). In practice, many policy notes (as well as staff reports) on FCS seem to have treated these countries almost like any other country, in a “pedestrian” way, as characterized by a former senior IMF staff member, focusing almost exclusively on headline macroeconomic trends and paying little attention to underlying institutional issues.⁴⁴

⁴² Staff highlighted the risk that the Chadian authorities, in a security-challenged region, might be tempted to use the oil revenue to boost military spending, and suggested that military spending be benchmarked to non-oil GDP; a quantitative performance criterion on wage spending included the military.

⁴³ In some cases, senior staff mentioned that mission chiefs could be “more ambitious” than SPR reviewers in responding to requests from reform-minded authorities wishing to bolster their agenda.

⁴⁴ In discussing this issue, some staff members pointed to the constraints imposed by limits on the length of staff reports. Arguably, some of the more mechanical and detailed elements of program content could be delegated to annexes, where there are no page limits, leaving more scope for the body of the report to concentrate on a fuller development of the overall strategy.