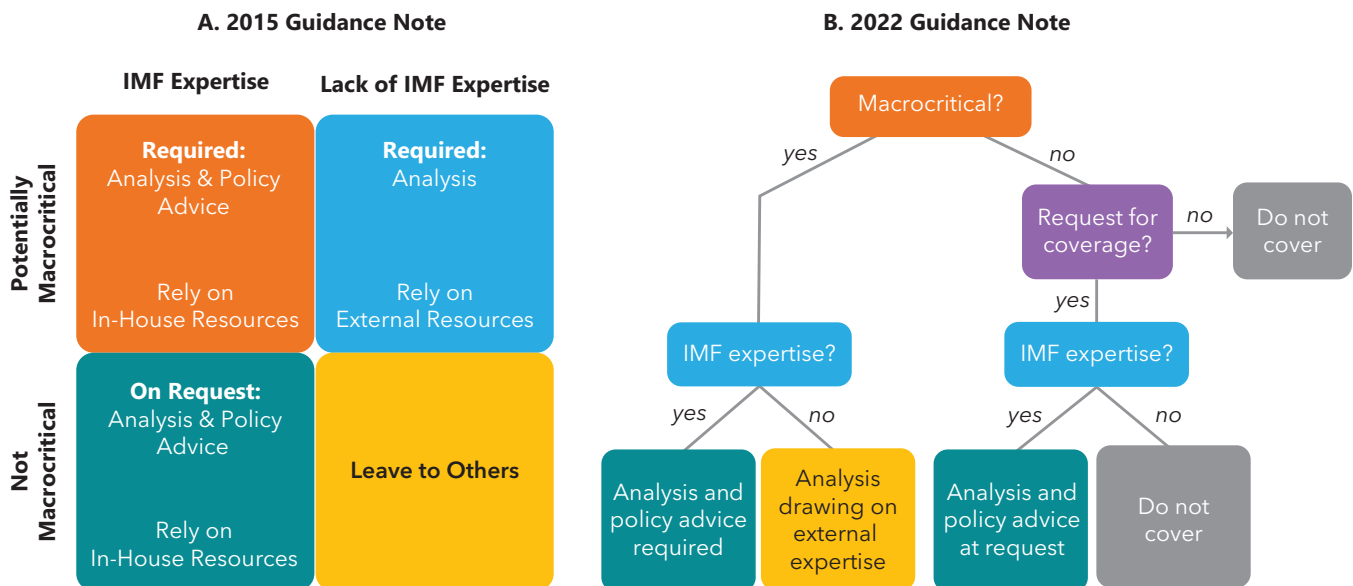


# ENHANCING CLARITY OF PRINCIPLES FOR ENGAGEMENT<sup>25</sup>

The IMF’s framework for engagement on structural issues was operationalized through a series of principles that were developed through different surveillance reviews, decisions, and guidance notes. The 2014 Triennial Surveillance Review (TSR) concluded that “[e]stablishing clearer principles for engagement would help avoid an ad hoc focus on structural issues. Principles or ‘filters’ could also help delineate the depth of the Fund’s involvement, namely when and when not to offer specific policy advice” (IMF, 2014b). Since then, the Fund has adopted specific principles and refined them through different guidance notes to enhance the relevance and value-added of the Fund’s engagement on structural issues (Figure 7). The 2015 Guidance Note embraced two specific principles as the basis for more systematic engagement: the principle of “macrocriticality,” which establishes the perimeter, i.e., when the Fund should engage, and the principle of “IMF expertise,” which determines whether the Fund should provide policy advice (IMF, 2015b). The 2021 Comprehensive Surveillance Review (CSR) proposed a new criterion, namely, “relevance, severity, and urgency,” to determine the depth and frequency of coverage (IMF, 2021c). Subsequently, the 2022 Guidance Note introduced this third filter to determine the depth of coverage, but it did not specify a filter to govern the frequency.

FIGURE 7. CRITERIA FOR COVERAGE OF STRUCTURAL ISSUES IN SURVEILLANCE



Sources: IMF (2015b) and IMF (2022a), respectively.

<sup>25</sup> This section draws on the background paper by Jannils and Wojnilower (2024).

**TABLE 3. OPEN QUESTIONS ABOUT THE PRINCIPLES FOR ENGAGEMENT**

OBJECTIVE	FILTER	OPEN QUESTIONS
Establish the Perimeter	Macrocriticality	<ol style="list-style-type: none"> <li>1. How should staff determine if a structural issue is macrocritical for a specific country?</li> <li>2. To what extent is coverage of macrocritical structural issues required?</li> <li>3. What time horizon(s) should staff consider when making their assessments of macrocriticality and economic sustainability?</li> </ol>
Provision of Policy Advice	IMF Expertise	<ol style="list-style-type: none"> <li>4. How should staff determine if the Fund has expertise on a particular structural issue?</li> <li>5. To what extent should staff provide policy advice when Fund expertise exists but supply is lacking?</li> <li>6. Should the IMF expertise filter be applied at all?</li> </ol>
Depth of Coverage	Relevance, Severity, and Urgency	<ol style="list-style-type: none"> <li>7. How should staff determine the relevance, severity, and urgency of a macrocritical issue, both independently and relative to others?</li> <li>8. What are the different depths of engagement?</li> </ol>
Frequency of Coverage	Unspecified	<ol style="list-style-type: none"> <li>9. How should staff determine when and how often to engage on a macrocritical structural issue?</li> </ol>
Uniformity of Treatment	Evenhandedness	<ol style="list-style-type: none"> <li>10. How should staff determine which “similar circumstances” are relevant when assessing evenhandedness?</li> <li>11. To what extent does the application of risk-adjusted inputs lead to outputs that both are and are perceived to be uniform in treatment?</li> </ol>

Source: IEO staff.

However, in trying to balance consistency and flexibility, this framework left open important questions about how these principles should be applied, which ultimately could affect the traction of surveillance (Table 3). While this framework is designed to limit the scope and increase the consistency of Fund engagement, the Board, management, and staff simultaneously have sought to ensure it also retained enough flexibility to cover new policy areas and adapt to country-specific circumstances. Consequently, this framework left open important questions regarding how the filters should be applied in Fund surveillance to achieve the desired objectives. Further, the five specific strategies adopted by the Fund depart from these principles in various ways, reducing clarity about this framework.<sup>26</sup> To the extent these questions remain open, they ultimately could affect the traction of the Fund’s surveillance, which primarily depends on members’ perceptions about the quality and relevance of the Fund’s analysis and policy advice. Additionally, traction depends on the extent to which members believe the Fund’s treatment is uniform, i.e., evenhanded. To enhance this concept’s clarity, the Board approved a framework for addressing

evenhandedness concerns which, nevertheless, also left open important questions regarding its application (IMF, 2016b).

The rest of this section focuses on the operationalization of the surveillance mandate through the different periodic surveillance reviews, guidance notes, and the five specific strategies for governance, social spending, digital money, climate change, and gender. It is structured around the principles of macrocriticality, expertise, depth, frequency, and uniformity of treatment, and results in key findings 7 and 8, summarized in Section 6.

### PERIMETER: WHAT IS MACROCRITICAL FOR SURVEILLANCE PURPOSES?

The 2014 TSR recommended macrocriticality remain as the first filter for establishing the perimeter of Fund engagement on structural issues, which was further operationalized in the 2015 Guidance Note and affirmed in the 2022 Guidance Note. Macrocriticality, in this case, reflected whether an issue or policy significantly influences

<sup>26</sup> These strategies did not modify the existing legal framework for surveillance, which is set forth in the ISD, but they did attempt to clarify how the ISD should be operationalized in their respective policy areas.

present or prospective BOP or domestic stability.<sup>27,28</sup> Nevertheless, the 2014 TSR cautioned that “[t]his single filter could imply a massive expansion of the Fund’s advice on specific structural issues, some of which fall beyond its expertise.” The Board endorsed the 2014 TSR’s recommendations, yet several Executive Directors sought clarification on how the recommendations would be implemented and called for a more detailed framework for assessing the macrocriticality of structural reforms (IMF, 2014c). Using the 2014 TSR’s recommended principles, the 2015 Guidance Note introduced a more detailed framework for assessing the macrocriticality of structural issues (IMF, 2015b):

- ▶ (i) “For structural issues that are *macrocritical* and where the Fund has *in-house expertise*, analysis and policy advice are required.”
- ▶ (ii) “For structural issues that are *macrocritical* but where *Fund expertise is lacking*, staff should analyze the issue, drawing on expertise from other organizations.”
- ▶ (iii) “For structural issues that are *not macro-critical* but for which the *Fund has expertise*, staff may provide analysis and policy advice when requested by the authorities.”
- ▶ (iv) “For structural issues that are *not macro-critical* and *Fund expertise is lacking*, analysis and policy advice should be left to other organizations.”

**While this framework is more detailed, it initially left open two important questions: (1) How should staff determine if a structural issue is macrocritical for a specific country; and (2) to what extent is coverage of macrocritical structural issues required?** On question (1), the 2015 Guidance Note directed staff to “exercise judgment and take into account country circumstances,” but offered little else in terms of practical guidance for making that determination. On question (2), the text of the 2015 Guidance Note differentiated between the terms “required” and “should” with regard to macrocritical structural issues. However, the corresponding figure (see Figure 7, left panel) converted the term “should” to “required” when referring to analysis of structural issues that are macrocritical, but where Fund expertise is lacking.

**This evaluation found a lack of clarity on both questions in the five specific strategies of governance, social spending, digital money, climate change, and gender.** On question (1), all five strategies lacked granular guidance about how to determine whether a particular structural issue is macrocritical in a particular country.<sup>29</sup> On question (2), four of the five specific strategies noted that Article IV consultations should cover macrocritical structural issues, however, their interpretations of that term differed.<sup>30</sup> The governance framework and social spending strategy, for example, emphasized that a discussion of macrocritical structural issues is required. The climate change and gender

<sup>27</sup> The term “macrocritical” has been used by the IMF dating back at least to the IEO’s first evaluation on the Prolonged Use of IMF Resources (IEO, 2002). In that instance, the term referred to the extent to which structural conditionality in IMF lending was “critical to achieving the programs’ macroeconomic objectives” (IEO, 2002). It also has been used in Article IV staff reports dating back to at least 2003. In the Article IV staff report on Ukraine that year, the term was used similarly in reference to structural conditionality in IMF programs (IMF, 2003). Subsequently, the term was used many times as a conditionality criterion in Fund reports on Poverty Reduction and Growth Facility (PRGF) arrangements. However, the term currently is clearly understood as a shorthand for the scope of bilateral surveillance set forth under the 2007 Decision and then the 2012 ISD.

<sup>28</sup> “In the Use of Fund Resources (UFR) context, while IMF staff routinely discusses with member authorities issues that are considered to be macrocritical, the establishment of program conditionality is subject to specific standards that do not refer to ‘macrocriticality.’ These standards are set forth in the Guidelines on Conditionality and state that conditionality should only be set on measures that are (i) critical for meeting program objectives or for monitoring the program’s implementation, or (ii) necessary for implementing specific provisions of the Fund’s Articles of Agreement or policies adopted under them” (IMF, 2019).

<sup>29</sup> The social spending and gender strategies deferred this content to future guidance notes specific to their respective policy areas, whereas the climate strategy deferred this content to the 2022 Guidance Note. The governance framework, in contrast, suggested the need for a guidance note would be obviated by its top-down approach to macrocriticality assessments. Furthermore, the digital money strategy did not specify a plan for it, as digital money issues were not considered to be macrocritical (though they were expected to become so in the future). Subsequently, and as of this writing (February 2024), the Fund produced the 2022 Guidance Note and a series of additional analytical work in various areas, including a how-to note on operationalizing IMF engagement on social spending during, and in the aftermath of, the COVID-19 crisis (IMF, 2020b). The Fund also created technical notes on pensions and social safety nets (IMF, 2022b; d), and an interim guidance note on mainstreaming gender (IMF, 2024a). While these guidance notes and analytical work offered far greater detail on how to engage, they still offered limited practical guidance on determining whether a particular structural issue is macrocritical in a particular country.

<sup>30</sup> The digital money strategy did not include a discussion of the macrocriticality requirements, potentially because digital money issues were not yet considered to be macrocritical.

strategies, by contrast, deemed the coverage of at least some macrocritical structural issues to be voluntary. This difference seemingly stemmed from a lack of sufficient resources to make coverage mandatory. Further, a gradual approach to implementing new strategies provides the Fund with the flexibility to identify best practices via a process of learning-by-doing.

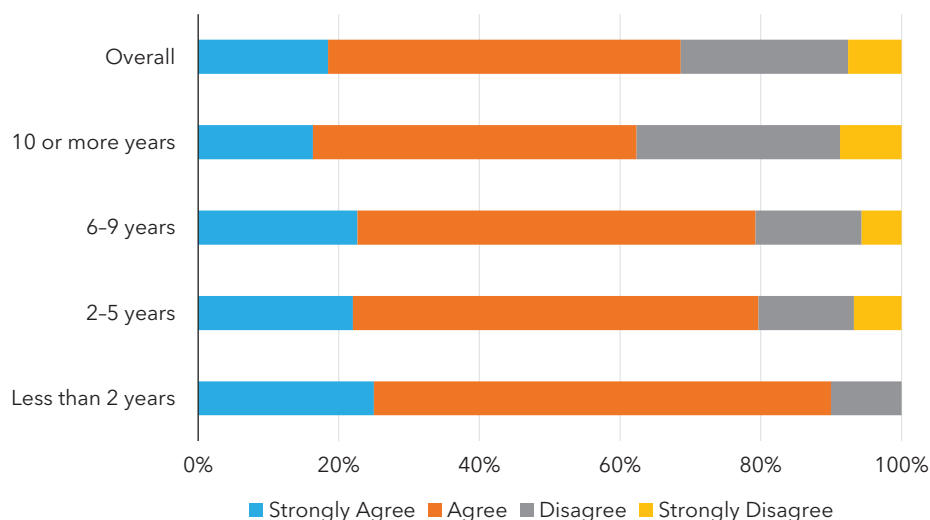
**While the Fund clearly has gone to great lengths to elucidate how to apply the concept of macrocriticality in surveillance, this evaluation found that enhanced clarity still is needed.** More specifically, the IEO survey’s results showed that a large minority of staff (31 percent) did not agree that a common understanding existed on how the concept of macrocriticality should be applied in IMF surveillance (Figure 8). The results also suggested the perception of a common understanding decline the longer someone works at the Fund. Interviews with Fund staff revealed a similar lack of clarity regarding the concept of macrocriticality. For example, many interviewees found the term too vague to implement in practice and expressed a desire for further clarification. Yet, highlighting the tension between flexibility and consistency, numerous staff also expressed a desire to retain a significant degree of judgment on whether an issue is macrocritical given country-specific

circumstances. Numerous Executive Directors, in interviews, expressed separate concerns that too many issues were being labeled as macrocritical, which has led to inconsistent engagement across structural issues and countries. Several Executive Directors proposed developing a clearer definition, yet, reflecting the tension between flexibility and consistency, acknowledged that such efforts should not prohibit the Fund from adapting its activities in response to global events.

**The 2021 CSR further broadened the perimeter of surveillance through the priority of fostering economic sustainability, which raised a third question: (3) What time horizon(s) should staff consider when making their assessments of macrocriticality and economic sustainability?** Following the Board’s approval of the 2021 CSR, the 2022 Guidance Note seemingly incorporated the concept of economic sustainability under the umbrella of macrocriticality. It defined economic sustainability “as a set of conditions that, under realistic assumptions, will support sustained, balanced, and inclusive growth, without requiring large or disruptive adjustments to the BOP or domestic stability.” Thus, the notion of prospective stability apparently was clarified to include the set of conditions that lead to economic sustainability. Here, Fund surveillance

**FIGURE 8. COMMON UNDERSTANDING OF MACROCRITICALITY**

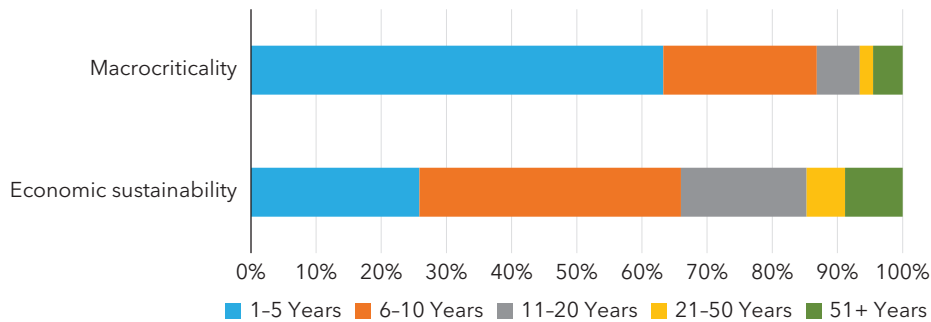
To what extent do you agree that most people working for the IMF have a common understanding of how the concept of macrocriticality should be applied in IMF surveillance?



Source: IEO survey of Fund staff.

## FIGURE 9. TIME FRAMES FOR SURVEILLANCE

In your view, the following concepts should be applied in IMF surveillance in which of the following time frames?



Source: IEO survey of Fund staff.

generally has focused on the short to medium term (1–5 years), which coincides with political cycles and the typical lengths of Fund programs.<sup>31</sup> However, the 2022 Guidance Note established that “[c]overage of issues related to economic sustainability may require a broader perspective and longer time horizon than has been typical for Fund surveillance.”

**While the Fund has tried to break down how the concept of economic sustainability should be applied in IMF surveillance, this evaluation finds that further effort is needed to enhance clarity among Fund staff.** Results from the IEO survey showed that while most respondents (63 percent) believed assessments of macrocriticality should be limited to the short to medium term, most respondents (74 percent) also thought assessments of economic sustainability should cover a longer time horizon than has been typical in Fund surveillance, i.e., more than five years (Figure 9). Moreover, staff broadly supported an array of time frames in each case. Interviews with Fund staff separately revealed a general lack of awareness that the 2021 CSR had established economic sustainability as a surveillance priority. Nevertheless, most respondents indicated that they had been engaging on structural issues related to economic sustainability since long before the 2021 CSR was published.

### POLICY ADVICE: WHAT IF IMF EXPERTISE IS LACKING?

**The 2014 TSR recommended IMF expertise as the second filter to determine whether the Fund should provide policy advice on structural issues.** This second filter was operationalized in the 2015 and 2022 Guidance Notes (see Figure 7). More specifically, for macrocritical structural issues, the IMF expertise filter delineated whether policy advice is required or not expected (notwithstanding that the issue should be covered without policy advice). For structural issues that are not macrocritical, the IMF expertise filter delineated whether or not policy advice should be provided.

**However, the IMF expertise filter initially left open two additional questions: (4) How should staff determine if the Fund has expertise on a particular structural issue; and (5) to what extent should staff provide policy advice when Fund expertise exists but supply is lacking?** On question (4), the 2022 Guidance Note mentioned “expertise” numerous times but was silent in terms of practical guidance. On question (5), the Fund’s past efforts to ramp up its work on macroprudential policy and macrofinancial analysis demonstrated that there are limits to how quickly and widely the Fund can build expertise on a broad topic.

<sup>31</sup> The ISD specifically states that the “Fund’s assessment of a member’s policies and its advice to a member will, to the extent possible, be placed in the context of an examination of the member’s medium-term objectives and the planned conduct of policies, including possible responses to the most relevant contingencies.” The 2022 Guidance Note, accordingly, mentions that “[s]taff reports should be based on realistic projections and discuss short- and medium-term objectives and policies as well as possible policy responses to the most relevant contingencies.”

The demand for expertise will therefore likely exceed the available supply for the foreseeable future, at least for some structural issues.

**This evaluation found a lack of clarity on both questions for the five specific strategies.** On question (4), the five specific strategies were sorely lacking in terms of offering practical guidance to staff on determining whether the Fund has expertise on a particular macrocritical issue. The subsequent analytical work and guidance notes also have left this question largely open. On question (5), the five specific strategies provided some discussion about where expertise will reside in the Fund, and how it will be organized. The strategies also revealed, at least implicitly, that the Fund’s expertise is lacking on some issues and unavailable in some instances. Nevertheless, the strategies and subsequent guidance notes offered minimal practical guidance on whether and how to proceed with policy advice on such occasions.

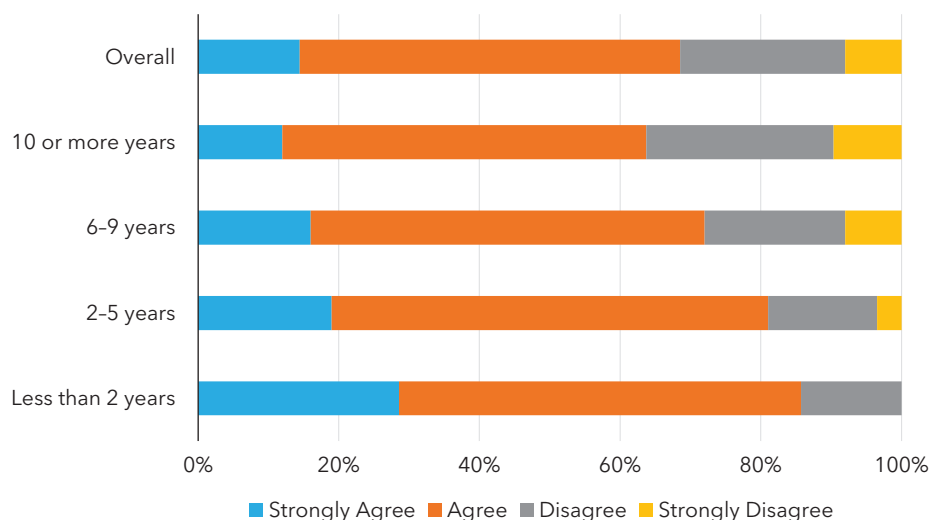
**Further, the five specific strategies raised an additional important question: (6) Should the IMF expertise filter be applied at all?** The governance framework and climate change strategy, for example, implied that the Fund should provide policy advice when their respective issues are deemed macrocritical, independent of whether

the IMF has expertise on a matter. The social spending strategy, meanwhile, appeared to use the IMF expertise filter to differentiate between general and specific policy advice, i.e., to provide general policy advice when a social spending issue is deemed macrocritical and the Fund lacks expertise, and to reserve specific policy advice for instances where the Fund has expertise. For gender issues, the interim guidance note implied that the expertise filter also should be used to differentiate between general and specific policy advice.

**While the Fund has attempted to explain how the concept of IMF expertise should be applied in surveillance, this evaluation found that enhanced clarity is needed.** More specifically, the IEO’s survey showed that a large minority of respondents (31 percent) did not agree that a common understanding exists on how the concept of IMF expertise should be applied in surveillance (Figure 10). The results also suggested that the perception of a common understanding declines the longer someone works at the Fund. Interviews with Fund staff revealed a similar lack of clarity regarding the concept. Several interviewees, for example, expressed concerns about the slow progress in hiring specialists and the challenges accessing specialized knowledge, given that demand often exceeds the limited supply. They also explained that the addition of new topics

**FIGURE 10. COMMON UNDERSTANDING OF IMF EXPERTISE**

To what extent do you agree that most people working for the IMF have a common understanding of how the concept of IMF expertise should be applied in IMF surveillance?



Source: IEO survey of Fund staff.



has strained country desks, as they seek to build expertise in these areas and learn to employ new analytical tools in addition to their previous responsibilities.<sup>32</sup> Several Executive Directors in interviews, expressed a separate concern that the Fund is providing detailed policy advice in areas where it lacks sufficient expertise, and that the Fund's increased efforts on these structural issues were impacting the quality of the Fund's analyses and policy advice in core areas. They called for greater clarity on the Fund's plans to develop internal expertise and collaborate with other international organizations, such as the World Bank.

### DEPTH: DEEP DIVES AND LIGHT TOUCHES

**The 2022 Guidance Note developed the criteria of “relevance, severity, and urgency” as a third filter to determine the depth of Fund engagement on structural issues, but left open two additional questions: (7) How should staff determine the relevance, severity, and urgency of a macrocritical issue, both independently and relative to others; and (8) what are the different depths of engagement?** The 2015 Guidance Note stated that not all macrocritical issues are expected to be covered in the same depth in every Article IV consultation. Thus, determining how deep that coverage should be required a different filter. The 2022 Guidance Note adopted the 2021 CSR's proposed criteria of relevance, severity, and urgency as the third filter. On question (7), the 2022 Guidance Note did not provide any additional details as to how these criteria should be defined or assessed. On question (8), the 2022 Guidance Note differentiated between in-depth coverage and updates on recent developments or references to previous reports, but did not go deeper (e.g., to describe what in-depth coverage entails).

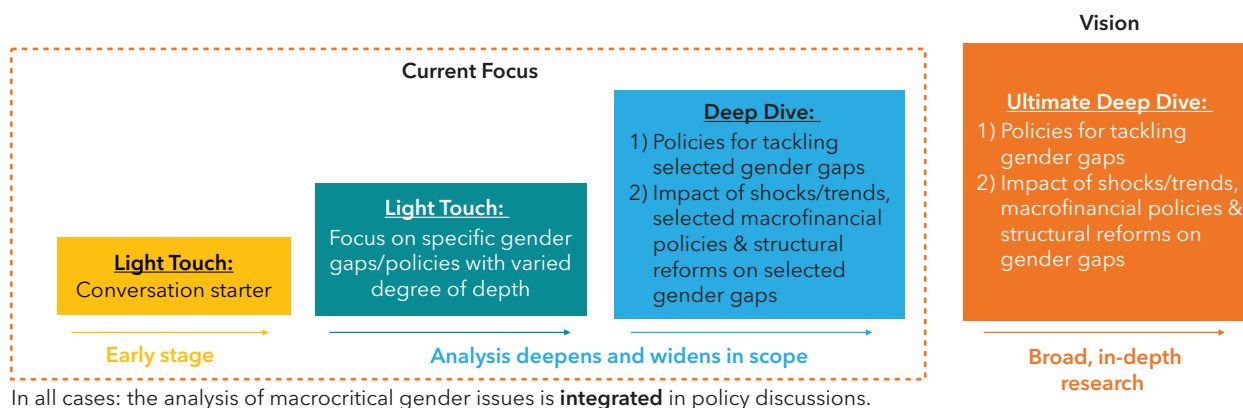
**This evaluation found a lack of clarity on both questions for the five specific strategies.** On question (7), as expected, this third filter was not covered in any of the four specific strategies that were completed before this filter was established (among them, only the social spending strategy even discussed an approach to determining the depth of policy advice). The gender strategy, which was completed after the 2022 Guidance Note, repeated the third filter verbatim, yet offered no additional details on how to define or assess these criteria. On question (8), only three of the five strategies discussed different depths of engagement. Two of those three—the digital money and climate change strategies—offered limited details on the different types of depth. The gender strategy, in contrast, created new terminology, i.e., “deep dives” and “light touches,” that was further developed in the interim guidance note on mainstreaming gender, which depicted a continuum of coverage differentiating between two types of deep dives and light touches (Figure 11). While this note provided “a more step-by-step approach” to gender coverage, it remains unclear as to how fully this taxonomy could be applied to other structural issues (IMF, 2024a).

**While the Fund has endeavored to clarify how the concept of depth should be applied in surveillance, this evaluation found that enhanced clarity still is needed.** The IEO's survey showed that most respondents (nearly 60 percent) did not agree that there is clear guidance on determining the relevance, severity, and urgency of a macrocritical issue (Figure 12). Separately, interviews with Fund staff revealed that the decision to conduct a light touch rather than a deep dive was based, at times, on a lack of access to the Fund's expertise, a lack of adequate data and indicators, or a country authority's willingness to engage.

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<sup>32</sup> The Fund's efforts to build and strengthen expertise included allocating resources to the newer policy areas, as discussed in Section 3, and kickstarting initiatives in terms of data and analytical tools and frameworks, which, in some cases, were joint ventures with other partners. For example, with regard to climate change, the Fund began developing expertise on carbon taxes early in the evaluation period and led efforts with the World Bank to build the Climate Policy Assessment Tool. The IMF also has striven to incorporate assessments of climate-related risks and climate stress testing in existing frameworks, such as FSAPs, Debt Sustainability Frameworks, and the External Balance Assessment-lite, as well as to create new tools, such as the Debt-Investment-Growth and Natural Disasters toolkit. Moreover, as improving data availability is fundamental to assessing newer policy areas, in 2021, the Fund, in collaboration with other partners, launched the Climate Change Indicators Dashboard, which could provide a useful precedent for other newer policy areas.

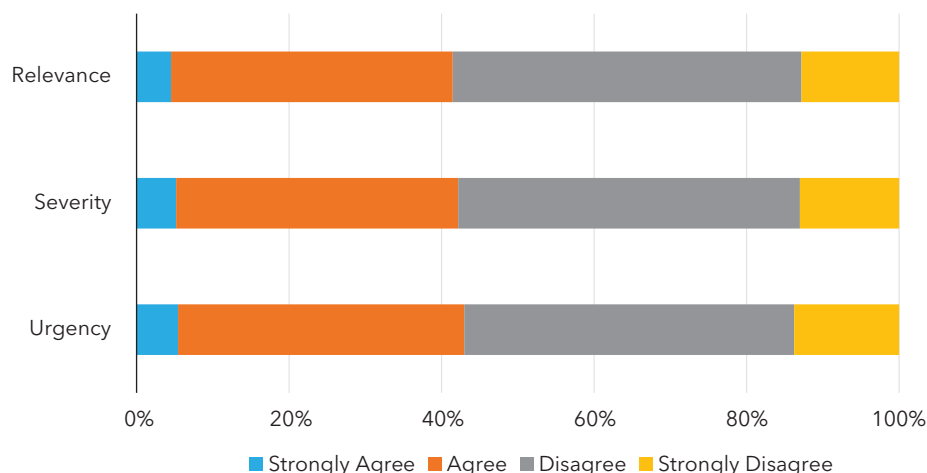
**FIGURE 11. TAXONOMY OF DEEP DIVES AND LIGHT TOUCHES**



Source: IMF (2024a).

**FIGURE 12. CLEAR GUIDANCE ON DEPTH OF COVERAGE**

To what extent do you agree there is clear guidance to IMF staff at the institutional level regarding how to determine the following conditions in IMF surveillance?



Source: IEO survey of Fund staff.

### FREQUENCY: A NEED FOR A NEW FILTER?

The 2022 Guidance Note did not establish a fourth filter to determine the frequency of coverage of structural issues and thereby left another important question open: (9) How should staff determine when and how often to engage on a macrocritical structural issue? The 2015 Guidance Note stated that not every macrocritical issue

must be included in every report.<sup>33</sup> Thus, determining when and how often that coverage should take place requires a different filter. The 2021 CSR proposed using the same set of criteria (i.e., relevance, severity, and urgency) to determine the depth and timing of coverage, yet the 2022 Guidance Note did not adopt those criteria or any others as the fourth filter.

<sup>33</sup> The 2022 Guidance Note, meanwhile, stated that “the ISD requires [macrocritical issues] to be discussed in Article IV consultations to the extent the Fund has expertise.”



**This evaluation found a lack of clarity on question (9) for the five specific strategies.** Only three of the five strategies discussed the frequency of engagement. Two of those three, the social spending and climate change strategies, only offered high-level guidance on the number of years within which the Fund should engage. The governance framework, in contrast, established criteria to determine the frequency of engagement, which included the urgency of the problem, a country’s specific circumstances, and other competing policy issues. While these criteria could constitute the fourth filter, it seems unlikely that they could be applied in a manner consistent with the uniformity of treatment principle.

**The lack of a fourth filter opens the door to several options, including the possibility of establishing a “new core.”** While the 2022 Guidance Note did not specify a fourth filter for all structural issues, it did contain another option. It discussed using the criteria of severity and urgency solely for macrocritical climate issues. Alternatively, this fourth filter could be obviated by bridging a gap in the ISD between traditional core policies and at least some newer policy areas. More precisely, the ISD affirmed that the Fund’s bilateral surveillance should always focus on traditional core policies, whereas newer policy areas would be subject to the macrocriticality test. A new surveillance decision could therefore elevate one or

more of the newer policy areas to the “core,” as was done with the financial sector in the 2007 Decision.<sup>34</sup> Another option would be to explicitly establish a requirement for newer macrocritical policies, to be covered within a specific time frame or with a sequencing framework. Furthermore, a new surveillance decision could bridge a gap in the ISD between bilateral and multilateral surveillance (Box 3).<sup>35</sup>

**Whether or not the Fund establishes a filter to determine the frequency of coverage, it will be important to ensure that the interdepartmental review process is consistent with Article IV guidance to avoid a checklist mentality.** While the Board, management, and staff appear to share a view that every macrocritical issue does not need to be included in each Article IV report, interviews conducted for this evaluation revealed general pressure from the interdepartmental review process to cover specific areas in every report.<sup>36</sup> An analysis of Article IV staff reports lends support to this perception, since nearly all reports covered governance, social spending, and climate change issues, at least to some extent, in the last two years of our data (Figure 13). Overcoming this perceived checklist approach may require a concerted effort by the Board, management, and staff reviewers in order to avoid an expectation of coverage, independent from a review of past Article IV reports and planned future examinations.

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<sup>34</sup> In 2006, *The Managing Director’s Report on Implementing the Fund’s Medium-Term Strategy* stated that the “coverage of financial sector issues in Article IVs needs to be elevated to a higher level ... to give financial issues coverage that is at least on par with, say, the traditional fiscal policy analysis found in Article IV reports” (IMF, 2006a). This suggestion was later formalized in the 2007 Decision (see Box 1, Section 2).

<sup>35</sup> Bossone (2024) elaborates on proposals to improve the ISD.

<sup>36</sup> There are different interdepartmental review processes for country work, policy work, Staff Discussion Notes (SDNs), and multilateral surveillance products. The steps involved in country work, which includes Article IV staff reports, broadly are as follows: (i) early engagement with SPR (and other relevant departments) to ensure that all relevant topics are covered in the initial draft; (ii) formal interdepartmental reviews, where reviewers produce comments that are focused on the areas for which their department is responsible; (iii) SPR clearance of the revised document to ensure the main comments have been addressed; and (iv) management review and clearance, “to mediate key departmental differences, make judgment calls on options,” and endorse the report (IMF, 2023e).

### BOX 3. COVERAGE OF CLIMATE CHANGE MITIGATION

As part of the 2021 CSR, the Board approved a background paper on integrating climate change into Article IV consultations (IMF, 2021f). This paper focused on three types of policy challenges: (i) mitigation; (ii) adaptation; and (iii) managing the transition to a low-carbon economy. The latter two types were deemed *domestic policy challenges*; thus, coverage was warranted under the ISD's bilateral surveillance provisions, "provided they cross the threshold of macro-criticality." On the other hand, this paper determined that "climate change mitigation is *not* primarily a domestic policy challenge" because an individual country's policies would be insufficient to prevent climate change on their own. Nevertheless, this paper pointed out that the global "macroeconomic relevance of climate change mitigation is beyond doubt."

This raised two important questions about the extent to which climate change mitigation can be covered in Article IV consultations under the ISD's multilateral spillover provision, which covers "domestic economic and financial policies that may significantly influence the effective operation of the international monetary system" (IMF, 2012):

- ▶ First, to what extent are climate change mitigation policies considered economic and financial policies and, if so, can the Fund cover the spillover effects from the absence of such a mitigation policy?<sup>1</sup> The CSR background paper implicitly answers this question affirmatively, thereby allowing for coverage of climate change mitigation policies, even in their absence.
- ▶ Second, how should the Fund determine if the spillover effects of a member's policies, or their absence, *significantly* influence the effective operation of the IMS? The CSR background paper acknowledged the difficulty in establishing a straightforward assessment and proposed a pragmatic approach. It *strongly* encouraged covering a country's contribution to the global mitigation effort for the 20 largest emitters of greenhouse gases<sup>2</sup> and, for all other countries, coverage was encouraged, but not necessarily expected. This proposal raised a debate at the CSR's Board discussion with numerous Executive Directors emphasizing that coverage should be voluntary and demand driven, i.e., at the request of country authorities.

The 2022 Guidance Note attempted to clarify the what, when, and how of the Fund's coverage of climate change mitigation issues, while affirming that coverage under multilateral surveillance would be "voluntary but strongly encouraged." The internal version of the 2022 Guidance Note added context to this notion by asking country teams for the top 20 emitters to discuss coverage of multilateral aspects of climate mitigation with the authorities, and, if the authorities were not willing to engage, to reflect the authorities' reservations in a back-to-office report. The internal 2022 Guidance Note did not clarify what should happen, if anything, beyond that step. Thus, questions remain regarding the expectation of coverage of climate change mitigation for the 20 largest emitters, as well as its depth and frequency.

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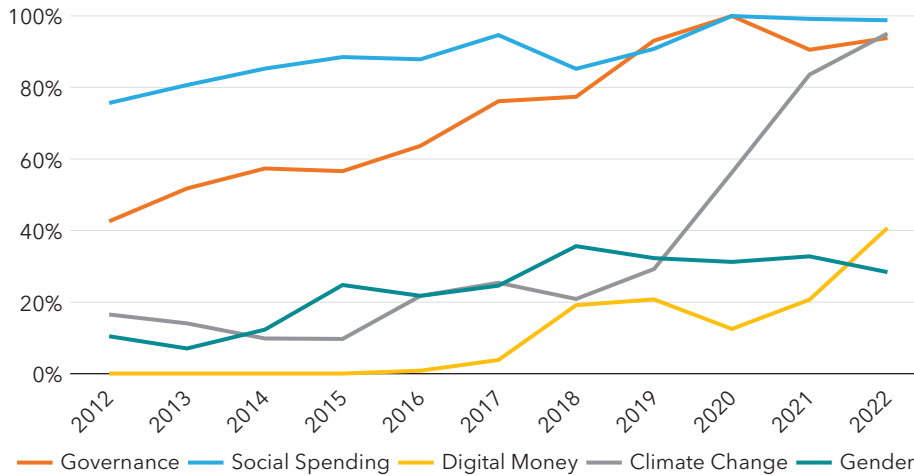
Source: Authors' assessment.

<sup>1</sup> In the Board minutes on the 2021 CSR and the climate change strategy, several Executive Directors expressed the view that at least some climate change mitigation policies fall outside the economic and financial realm and therefore extend beyond the Fund's expertise and mandate (IMF, 2021g; j).

<sup>2</sup> The background paper noted the existence of valid concerns as to whether current greenhouse gas emissions constitute an appropriate standard for determining significance. In the accompanying Board minutes, as well as the Board minutes on the climate change strategy, several Executive Directors took issue with using this yardstick and expressed a preference for factoring in a country's historical contributions to the emission of greenhouse gases (IMF, 2021g; j).

## FIGURE 13. COVERAGE OF STRUCTURAL ISSUES IN ARTICLE IV STAFF REPORTS

(In percent of Article IV consultations)



Source: IEO staff calculations.

Note: This chart shows the percentage of Article IV staff reports containing at least three paragraphs covering each issue. The analysis utilizes the Fund Document Extraction Tool (FDET) developed by the Information Technology Department. This chart covers all 1,192 Article IV reports available in FDET for the period 2012–22.

### UNIFORMITY OF TREATMENT: A NEW APPROACH TO ASSESSING EVENHANDEDNESS?

**Traction of the Fund’s policy advice, which is a main objective of its surveillance, partially depends on the extent to which members believe the Fund’s treatment is uniform, i.e., evenhanded.** The objective of “uniformity of treatment” has been operationalized via the concept of “evenhandedness.”<sup>37</sup> The ISD stated that the Fund “will be evenhanded across members, affording similar treatment to members in similar relevant circumstances.” When the Board approved the ISD, the accompanying Board minutes reflected a concern about the extent to which Fund surveillance could be applied consistently, i.e., in an evenhanded manner, while maintaining sufficient flexibility to adapt to country-specific circumstances (IMF, 2012). The 2014 TSR recommended a new approach to assessing evenhandedness based on inputs to rather than outputs from surveillance. Inputs refer to resources, such as the number and experience of staff, as well as the depth of analysis. Outputs from surveillance, meanwhile, refer

to the particular policy advice and the way it is presented. Management and staff subsequently proposed a framework for addressing concerns related to the evenhandedness of Fund surveillance (IMF, 2016b).

**The 2016 evenhandedness framework left open two important questions: (10) How should staff determine which “similar circumstances” are relevant when assessing evenhandedness ...** The definition of evenhandedness in the 2016 framework departed slightly from the one contained in the ISD, when it noted that “countries in similar circumstances should be treated similarly.” In other words, it omitted the term “relevant” as a qualifier for “similar circumstances,” thereby widening the filter. This raised an important question because the overall circumstances facing every individual member country are unique, at least to some extent. So, in principle, an approach that excludes a relevance filter could imply that any pair of countries could be treated differently and still meet the evenhandedness criteria. On the other hand, with the narrower relevance filter, treating two countries differently on a specific structural issue would

<sup>37</sup> The specific notion of uniform treatment was mentioned at least as far back as the 2002 Guidelines on Conditionality, which state that the “Fund will ensure consistency in the application of policies relating to the use of its resources with a view to maintaining the uniform treatment of members” (IMF, 2002).

be evenhanded only if the country circumstances relevant to that particular issue are different.<sup>38</sup> The 2022 Guidance Note, when discussing evenhandedness, stated that “relevant country circumstances can include, but are not limited to, the income level, fragility and vulnerability of the members, institutional capacity, data adequacy, and whether the country member is engaged in Fund-supported programs or is a member of a currency or other economic union.” While this formulation of the evenhandedness concept helped reconcile the omission of the term “relevant” in other instances, it did not offer staff any practical guidance on determining which of those country circumstances would be relevant for assessing evenhandedness on a specific issue.

**... and (11) to what extent does the application of risk-adjusted inputs lead to outputs that both are and are perceived to be uniform in treatment?**<sup>39</sup> In the framework’s Summing Up, Executive Directors “emphasized that the ‘outputs’ of surveillance—effectively, the Fund’s policy analysis and advice as well as their presentation—should continue to be the primary basis for gauging evenhandedness” (IMF, 2016a). This reflected a concern that applying evenhanded risk-adjusted inputs could result in surveillance outputs that either are or are perceived to be lacking in uniformity of treatment. The 2022 Guidance Note provided some additional details to encourage greater consistency in risk-adjusted inputs, which “could include choices about: (i) the focus of resources; (ii) the depth of risk and spillovers analysis; (iii) the analytical approaches and tools; (iv) the selection of policy themes; and (v) the approach

to contentious issues.” These choices, nevertheless, imply that the Fund could evenhandedly differentiate its policy advice between countries facing similar circumstances, solely based on the issues being more contentious for one country’s authorities. The Executive Directors’ and authorities’ persistent concerns about a lack of evenhandedness suggest that such differentiated outputs would at least be perceived as failing to adhere to the uniformity of treatment principle.

**This evaluation found a lack of clarity on both questions surrounding the five specific strategies.** On question (10), only the governance and gender strategies addressed this question, and each took a different approach.<sup>40</sup> On question (11), the five specific strategies each referred to the goal of making surveillance evenhanded, but rarely mentioned the input-based approach or offered practical guidance to staff on how to ensure countries are treated uniformly.

**While the Fund evidently sought to clarify how the concept of evenhandedness should be assessed in surveillance, and to promote a consistent use of risk-adjusted inputs, this evaluation found that enhanced clarity still is needed.** More specifically, results from the IEO’s survey showed that nearly half of respondents (46 and 48 percent, respectively) did not agree that the macrocriticality test or the determination of whether the IMF has expertise were conducted in an evenhanded manner across the five newer policy areas (Figure 14). Fund staff, in interviews, also acknowledged difficulty assessing evenhandedness, given the number of different factors that informed their decisions on when and how to engage on structural issues.

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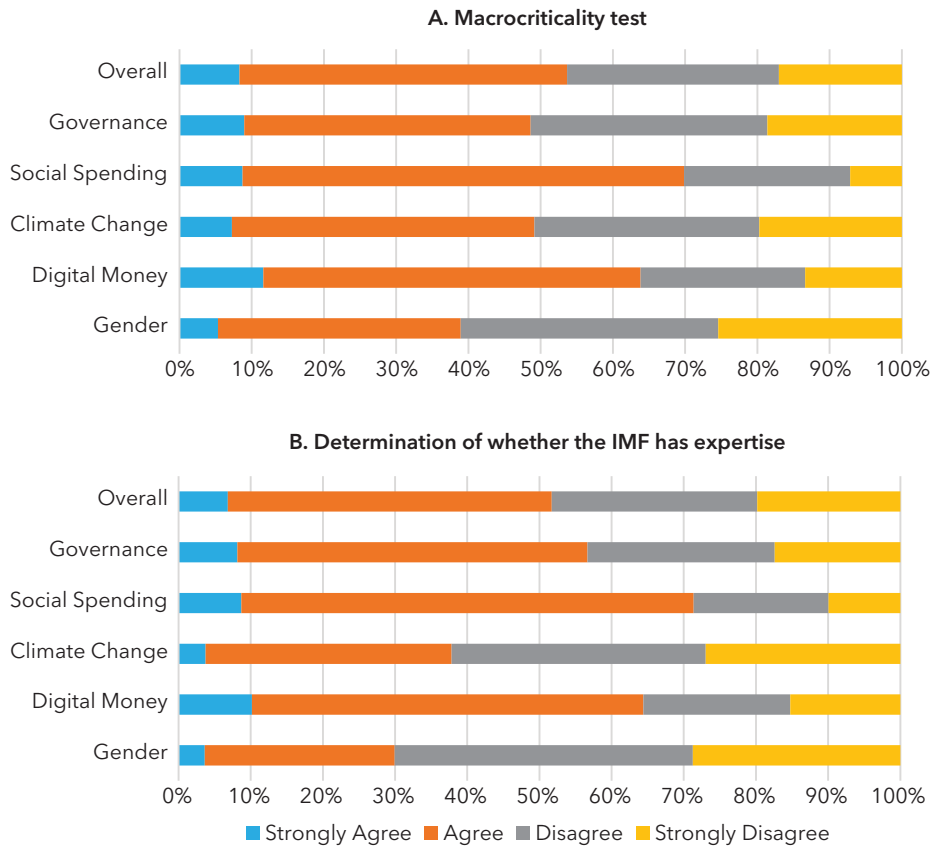
<sup>38</sup> For example, the governance framework called for “a centralized, institutional process to ensure that similarly-situated countries (in terms of their governance vulnerabilities) are treated similarly” (IMF, 2018b). In this context, a country’s region or income level would seem to be largely irrelevant to assessing governance vulnerabilities. Nevertheless, in reviewing the 1997 Guidance Note, many Fund mission chiefs expressed a view that the Fund lacked evenhandedness in addressing governance vulnerabilities, either because “the Fund was more lenient towards countries from certain regions,” or it “tended to overlook corruption problems ... in advanced economies.” Country authorities similarly cited a “lack of discussion of corruption in advanced economies” as indicating a lack of evenhandedness (IMF, 2017b). These perceptions would reflect a formal lack of evenhandedness only if a narrower relevance filter were applied, so that similar governance vulnerabilities would require similar treatment, irrespective of region and income level.

<sup>39</sup> “Risk-adjusted,” in this case, refers to inputs that account for “risks to a country’s own domestic and external stability, as well as global economic and financial stability” (IMF, 2016b).

<sup>40</sup> As seen in footnote 38, the governance framework aimed to ensure that similarly-situated countries (in terms of their governance vulnerabilities) are treated similarly, while the gender strategy, in contrast, suggested that “[c]ountries in similar circumstances should be treated in a similar manner, considering domestic and cross-country risks, resource constraints, the availability of analytical tools and data, and coverage of different policy themes” (IMF, 2022c).

## FIGURE 14. EVENHANDEDNESS

To what extent do you agree that \_\_\_\_\_ was conducted in a manner consistent with the uniformity-of-treatment principle (i.e., evenhandedness) in the following areas?



Source: IEO survey of Fund staff.