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Independent Evaluation Office  
of the International Monetary Fund

# BACKGROUND PAPER

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## **The IMF and Capacity Development— Case Studies for Asia**

Daniel Citrin and Christopher Legg

**IEO Background Paper**  
Independent Evaluation Office  
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Daniel Citrin\* and Christopher Legg†

July 27, 2022

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

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**ABBREVIATIONS**

ACES	Analytical Cost Estimation System
ADB	Asian Development Bank
APD	Asia and Pacific Department (IMF)
BI	Bank Indonesia
BRI	Belt and Road Initiative
CBIRC	China Banking and Insurance Regulatory Commission
CD	Capacity Development
CDMAP	Capacity Development Management and Administration Program
CDD	Capacity Development Department
CDOT	Capacity Development Office in Thailand
CICDC	China-IMF Capacity Development Center
CSN	Country Strategy Note
CSRC	China Securities Regulatory Commission
EFF	Extended Fund Facility
FAD	Fiscal Affairs Department (IMF)
FSAP	Financial Sector Assessment Program
FSSR	Financial Sector Stability Review
FTE	Full-Time Equivalent
GDP	Gross Domestic Product
HQ	IMF Headquarters (IMF)
ICD	Institute for Capacity Development (IMF)
IRA	Internal Revenue Act (Sri Lanka)
JICA	Japan International Cooperation Agency
LEG	Legal Department (IMF)
LoU	Letter of Understanding
LTX	Long-Term Expert
MCDF	Multilateral Center for Cooperation of Development Finance
MCM	Monetary and Capital Markets Department (IMF)
MoF	Ministry of Finance
MoU	Memorandum of Understanding
NBS	National Bureau of Statistics (China)
NDRC	National Development and Reform Commission (China)
OJK	Otoritas Jasa Keuangan (Indonesian Financial Services Authority)
PBoC	People's Bank of China
PFM	Public Financial Management
PRC	People's Republic of China
RBM	Results-Based Management
RCDC	Regional Capacity Development Center
RSN	Regional Strategy Note
SARTTAC	South Asia Regional Training and Technical Assistance Center

SAT	State Administration of Taxation (China)
SDDS	Special Data Dissemination Standard
STA	Statistics Department (IMF)
STI	Singapore Regional Training Institute
STX	Short-Term Expert
TA	Technical Assistance
TIMS	Travel Information Management System (IMF)
TSA	Treasury Single Account
UN	United Nations
VAT	Value-Added Tax
WEO	World Economic Outlook

## OVERVIEW

The four Asian case studies presented in this study aim to provide evidence and analysis to inform the IEO evaluation of IMF capacity development (CD) activities. The countries covered by this study have all had a significant engagement with the Fund during 2012–2020, the period covered by this study. Asia was the second largest user of IMF CD, after Africa, and within Asia, China was the second largest user, Cambodia the fourth, Sri Lanka the fifth, and Indonesia the eleventh over this period (Table 1).

	Cambodia	China	Indonesia	Sri Lanka
CD Missions (Total, 2012–2020, TIMS)	330	236	155	221
CD in FTE/Year (FY2012–2021, TIMS)	4.8	2.5	2.0	2.9
CD FTE (percentage of APD FTEs, FY2012–2021, TIMS)	8.0	4.1	3.3	4.8
CD intensity rank (compared to other APD, FY2012–2021, ACES)	4	2	11	5
CD intensity rank (compared to all recipients, FY2012–2021, ACES)	11	3	42	19
Training participant weeks/year (FY2012–2021, PATS)	249.8	484.1	267.3	180.7
GDP per capita PPP (USD, 2019, WEO)	4,832.7	16,659.5	12,482.8	13,622.9
Rank GDP per capita (2019, WEO)	148	80	106	96
Population (million, 2019, WEO)	15.6	1,400.1	266.9	21.8
UN Human Development Index (rank, 2020, UN)	144	85	107	72
Government Effectiveness Indicator (rank, 2019, World Bank)	143	60	84	109

Source: IEO staff calculations.

At the same time, the nature of these countries' challenges and their relationships with the Fund have differed from various perspectives.

- Cambodia underwent a significant transition from a planned to market economy, reaching middle income status in 2015. While it had program relationships with the Fund in the past (during 1999–2005), over the past decade engagement has been in a surveillance context. That said, the Fund has assisted Cambodia's transition process with extensive CD activities.
- People's Republic of China (PRC) is the largest systemically important economy with which the Fund has an active and growing CD relationship. The Fund has sought to respond to the authorities' demonstrated appetite for exploring international experience in market-based policy and regulatory systems and its potential relevance to Chinese circumstances. CD is also integral to Fund efforts to strengthen the broader relationship given PRC's growing global presence and relevance to the Fund's mandate.
- Indonesia, a large emerging economy of systemic importance, has had a surveillance relationship with the Fund since exiting from its post Asian crisis program in 2004. Nevertheless, the Fund provided significant CD covering broad policy reforms and

responses to particular financial issues as well as assistance of a more specific technical nature.

- Sri Lanka continued to experience significant macroeconomic and financial instability, and the country had a program relationship with the Fund over much of the period under review. Notably, the Extended Fund Facility (EFF) arrangement agreed in 2015 entailed wide-ranging reforms supported by IMF technical assistance (TA).

In line with the Fund's intention to enhance the integration of CD with surveillance, the Asia and Pacific Department (APD) has adopted a four-pillar strategy to prioritize the integration of CD into the surveillance and program work of its country teams, consisting of:

- Pillar I—Designing check points for CD issues in APD senior staff review of country papers and giving greater prominence of CD-surveillance links in Policy Notes and Staff Reports;
- Pillar II—Enhancing cooperation and synergies with CD-Delivery departments;
- Pillar III—Increasing the role of Regional CD Centers in on-the-ground engagement, including involving relevant experts in surveillance/program country work; and
- Pillar IV—Incentivizing surveillance-CD integration through the annual performance review process.

APD staff have produced country-specific strategies in various forms. Until 2015, country teams prepared annual notes reflecting APD's CD strategy for each individual APD recipient of CD. In 2015, the department sought to streamline by shifting to the preparation of CD matrices that summarized the country strategy, though country teams had discretion to prepare full-fledged strategy notes. Following the Fund's 2018 CD strategy review, Country Strategy Notes (CSNs) were required for all heavy CD users (IMF, 2018c). APD prepared such CSNs for Cambodia, China, and Sri Lanka (but not for Indonesia). Throughout the evaluation period, country CD priorities were reflected in APD's annual Regional Strategy Notes (RSNs), which were used to guide CD planning discussions with CD departments (CDDs).

The review of the four country cases covered in this study suggest that APD's country-led integration has achieved considerable progress and is strongly supported by the authorities as well as by staff in IMF CDDs. CD integration contributed to the effectiveness of the IMF's engagement by promoting the consistency between IMF CD and the key challenges facing the members. For both Cambodia and Sri Lanka, the planning and monitoring of comprehensive CD strategies have been a key part of the work of APD-led country team's work for some time. CD planning also reflected the close engagement of the authorities. In Indonesia's case, integration was less advanced, with CD activities mainly as a result of requests for TA or training in specific areas rather than an outcome of a comprehensive prioritization developed jointly by the authorities and the staff. This relative lack of integration appears to reflect lingering political

sensitivities regarding strategic engagement with the IMF in Indonesia. Nevertheless, the CD that was delivered was related to important policy issues, and in those areas coherent reform strategies were developed with the full involvement of the authorities. In the case of China, a robust internal Fund coordination process appears to have been effective in ensuring alignment of CD with surveillance priorities.

The CD delivered by the Fund was regarded by the authorities to be of high quality and generally well-tailored to country circumstances. In the cases of Cambodia, Indonesia and Sri Lanka, the authorities were satisfied that increasing attention was paid to hands-on assistance and training to facilitate the implementation of TA recommendations, particularly during the latter half of the period under review. In the case of PRC, the Fund developed a number of highly valued bespoke delivery mechanisms, underpinned by a series of Memorandums of Understanding (MoUs) and Letters of Understanding (LoUs) agreed with counterpart agencies to facilitate ownership and dialogue on priorities. In all four cases, the authorities generally felt that their feedback and input was taken into account during the delivery stage (as well as in the planning phase).

A number of factors contributed to success in delivery and follow-up. First, the authorities point to the continuity of experts, who could develop knowledge of country circumstances as well as personal relationships with counterparts, as a key element. Second, the efforts of IMF resident representatives in all four countries were also critical in the coordination and follow-up process. Third, in particular in Cambodia and Sri Lanka, where capacity was relatively weak, experts and advisors located in the IMF Capacity Development Office in Thailand (CDOT), the South Asia Regional Training and Technical Assistance Center (SARTTAC), and Regional Capacity Development Centers (RCDCs) offered timely and flexible assistance unencumbered by time zone differences and travel distance, and could also develop close relationships and experience in countries and the region. In PRC, tailored training delivered through the jointly funded China-IMF Capacity Development Center (CICDC) has been a key pillar of the CD relationship with the Fund. Finally, long-term resident advisors who can provide ongoing assistance and training are highly valued by the authorities in Asia, although care should be taken that: (i) given the investment they are truly welcomed and utilized by the host institution; and (ii) they not be regarded as “substitute employees” rather than “complements” to help build domestic capacity.

The review of country cases reveals a host of CD activities that have been owned by the authorities, in line with their priorities and needs, delivered effectively, and had a sustained impact. At the same time, experience in Cambodia, Indonesia and Sri Lanka points to cases where ownership has been weak or subject to shifting political circumstances, thereby leading to weak implementation or little sustained impact. Such instances have occurred in the context of both program and surveillance engagements between the member and the IMF. In a program situation, CD can play an important supportive role to the success of the lending arrangement, but close linkage to conditionality can heighten the risk that ownership will dissipate and implementation of recommendations cease due to political circumstances. And even in a surveillance context, close and explicit integration could heighten sensitivities associated with

accepting CD. The difficulties of measuring effectiveness and impact are particularly acute in the case of PRC, where the Fund's CD engagement is about helping the authorities to learn about alternative approaches and best practices and developing relationships and influence over the medium term, rather than delivering more standard CD outputs. The Fund's ability to engage on a sensitive issue such as debt sustainability in the context of the Belt and Road Initiative (BRI) underscores the potential value of continuing sustained efforts to build high level relationships of trust with the world's second largest economy and largest trading nation.

Transparency is a key value underpinning Fund accountability but has to be pursued in the context of respect for the member's sovereignty. In the cases of Cambodia, Indonesia and Sri Lanka, the authorities understood the general benefits of being able to learn from the experience of peers but with only a few exceptions declined to publish Fund TA reports, due to concerns about the release of sensitive information. In the case of PRC, Fund staff had little expectation that the authorities would consent to the public dissemination of CD reports or related materials and saw little point in using relationship capital to argue in favor of public release. However, Fund CD reports are disseminated and discussed widely within the Chinese government system, including at provincial level where the subject material is relevant.

The use of virtual modes of engagement since the onset of the COVID-19 pandemic was challenging in all four cases because of time zone differences. Internet connectivity was good in the cases of Indonesia and PRC, but presented significant difficulties to CD delivery to Cambodia and Sri Lanka. The authorities acknowledged that virtual CD was unavoidable in the circumstances but consider it no substitute for face-to-face interactions. In particular, the pandemic appears to have undermined the sustained investment in relationships needed to underpin the effectiveness of the MoU/LoU architecture built over recent years in PRC.

Against that background, the case studies suggest a number of ways in which the effectiveness of CD activities could be enhanced.

- Although forward-looking discussion of CD priorities has been in line with key challenges identified in surveillance, medium-term CD plans do not appear to be rigorously informed by results in the implementation of previous CD activities and recommendations. Making ex post assessments of previous delivery efforts an integral part of the planning process, with risk mitigation strategies in situations where prior implementation has been weak, would seem important to facilitating effectiveness and traction.
- At the same time, the establishment of early and ongoing milestones in the implementation of TA recommendations, and check-ins against expected outcomes, would help to ensure ownership and appropriate attention to country circumstances. Results-Based Management (RBM) methodologies used by CDDs to track implementation do not appear to be consistently discussed with country teams as well as the authorities as a way to promote ownership or guide prioritization.

- Newly available tools to manage the planning and governance of CD should help country teams integrate CD in their work, including in facilitating follow-up to TA recommendations, and also help Executive Directors support implementation. In this regard, much rests on the success of the IMF's Capacity Development Management and Administration Program (CDMAP) project, as it becomes fully operational.
- The efforts of suitably opportunistic and entrepreneurial resident representatives, drawing on local knowledge and relationships, can help nudge demand on key issues, as well as helping to coordinate and follow up CD delivery. Thus, the resident representative role is likely to remain highly valuable for addressing gaps and enhancing coherence over time.
- Notwithstanding best efforts, it may be inevitable in many cases that ownership will be swayed by changing political circumstances and will need to be built or re-built over time. And in addition, that the strengthening of institutional and human capacity may entail an extended process. In such cases, e.g., the tax administration project in Cambodia, recommendations need to be appropriately calibrated, with the scope and pace of reforms more modest. The focus in certain situations of weak implementation may need to be solely on more basic capacity building and training.
- In cases where there are broad and potentially controversial reforms to institutional or policy frameworks, it may be helpful to incorporate in the CD outreach efforts to build ownership among a wide range of stakeholders. Such efforts would need to pay due regard to any sensitivities and stigma regarding external advice. In a related vein, where feasible, collaboration with local expertise and partners, taking advantage of local relationships and knowledge, could be a helpful innovation.
- Finally, on the side of internal human resource incentives, greater rigor and consistency in defining performance expectations on CD issues and then applying them in annual assessments would be desirable. Notwithstanding good progress on APD four-pillar strategy, the integration of CD into the work of the country team still appeared to depend to a certain extent on the personal initiative and priorities of the mission chief.



# **CAMBODIA**

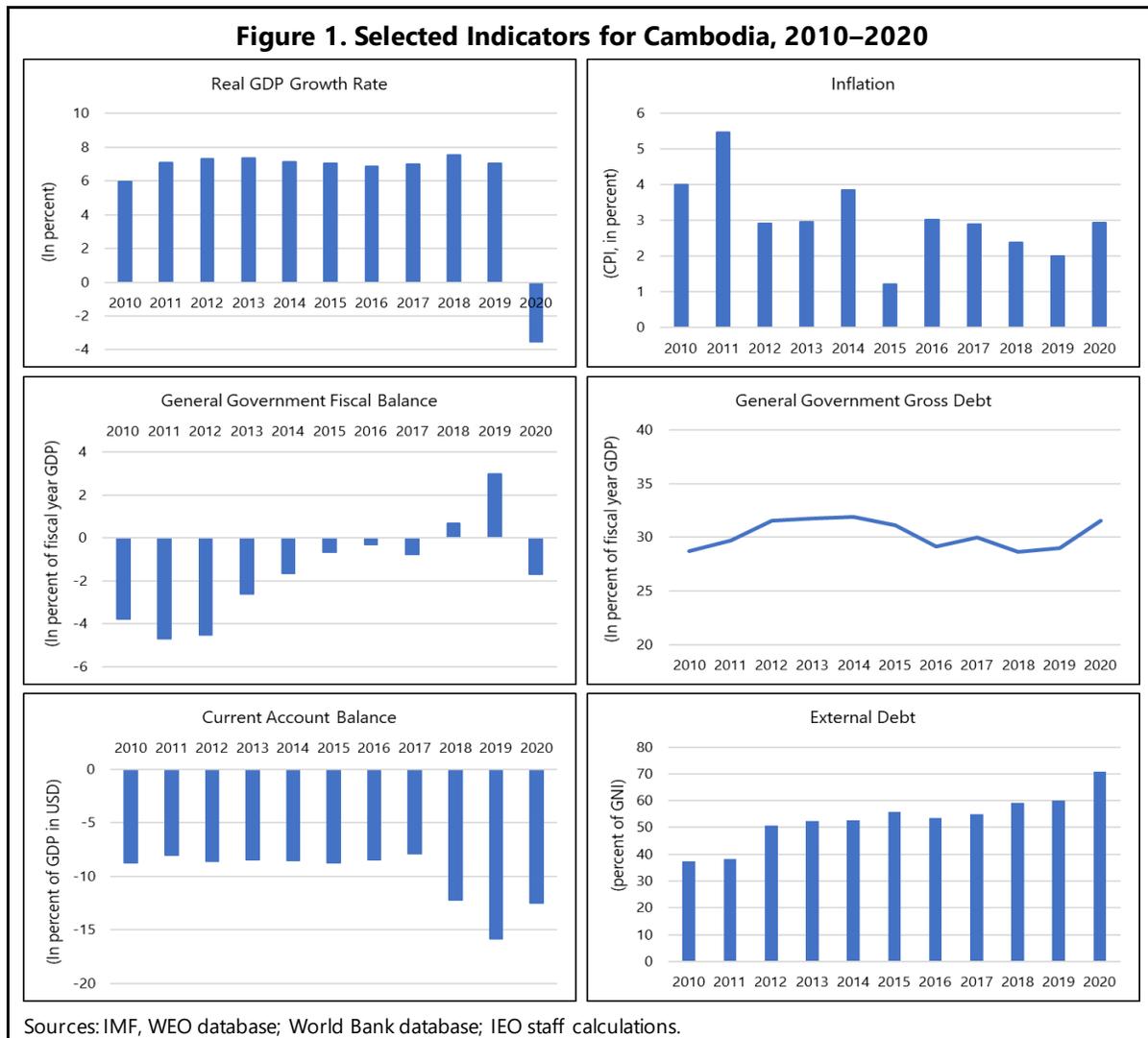
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## I. INTRODUCTION AND COUNTRY OVERVIEW

1. Cambodia has had an impressive macroeconomic performance over the past two decades, but significant challenges remain. During 2012–2019, real GDP growth averaged around [7 percent], inflation remained in the low single digits, and the overall fiscal situation improved significantly, with the budget moving into surplus in 2018–2019 (Figure 1). Cambodia reached middle-income status in 2015, while also making a significant transition from a planned to market economy. In 2020, like other countries in the region, Cambodia was hit hard by the global slowdown and associated effects of the COVID-19 pandemic. Real GDP contracted by 3 percent as foreign tourist arrivals came to a virtual halt and export orders fell sharply. Growth has recovered since but only gradually, as community spread of the virus in early 2021 led to tight domestic containment efforts.



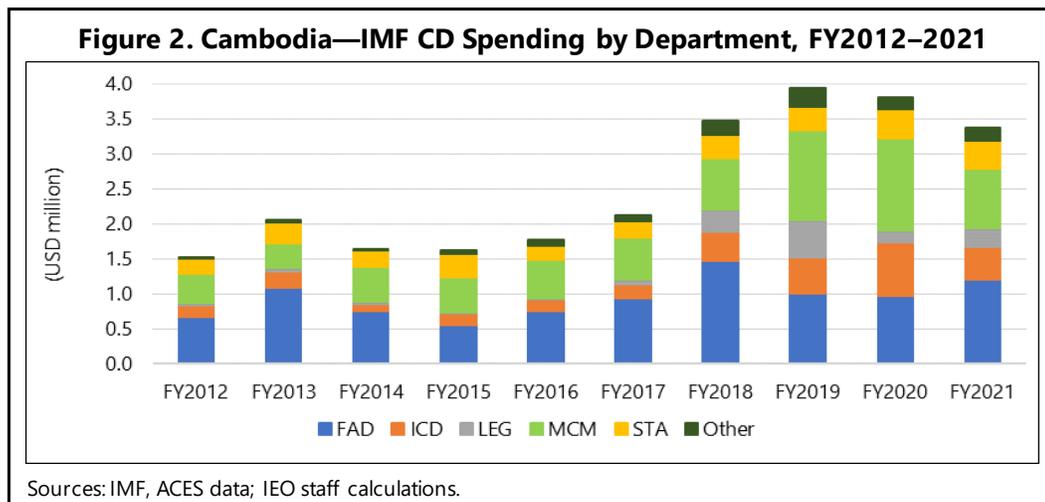
2. Cambodia faces significant challenges in generating strong and sustainable growth with financial stability in the years ahead. Financial vulnerabilities have been elevated in recent years by rapid credit expansion, particularly related to real estate, large infrastructure and social

spending needs confront fiscal policy, and the medium-term growth outlook is constrained by structural weaknesses such as a level low of competitiveness and weak business climate.

3. Cambodia has made substantial progress towards the sustainable development goals, but considerable efforts will be needed to meet the 2030 goals. Cambodia lags its regional peers on a range of indicators related to the availability and quality of education, health, and infrastructure.<sup>1</sup> And notwithstanding rapid growth, per capita income remains relatively low. Finally, looking ahead, Cambodia is also highly vulnerable to climate change, given the importance of agriculture and tourism. A comprehensive framework of structural reforms to improve competitiveness and diversify the economy, improve the business climate, strengthen economic governance, and step up social and infrastructure spending including through better efficiency in public spending are key to Cambodia's long-term economic development.

4. The IMF has assisted Cambodia's transition and development process with extensive capacity development (CD) activities. While Cambodia has had program relationships with the Fund in the past (during 1999–2005), over the past decade the engagement has been in a surveillance context. CD activity ramped up substantially since FY2017, and Cambodia was the eleventh largest user of IMF CD during 2012–2020 as a whole (see Table 1 in Overview).

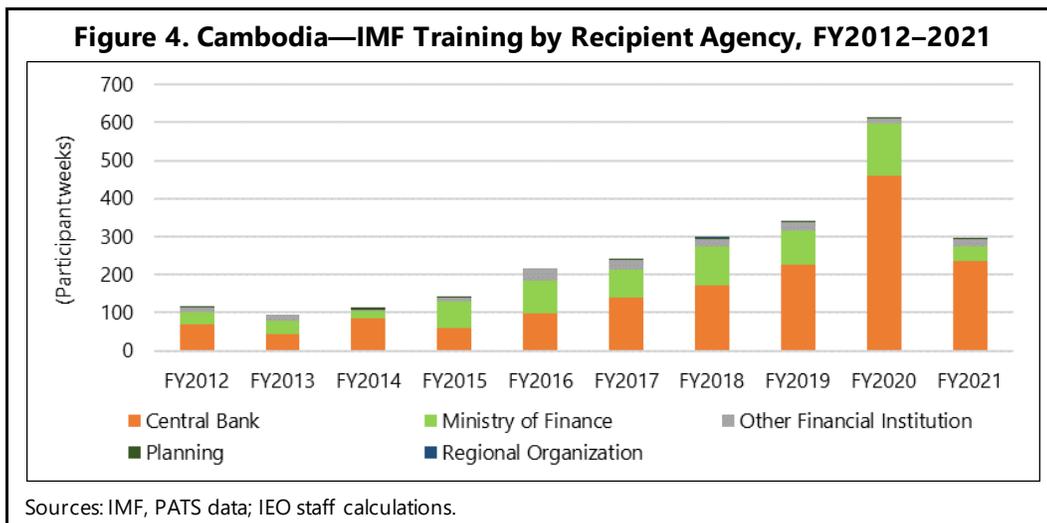
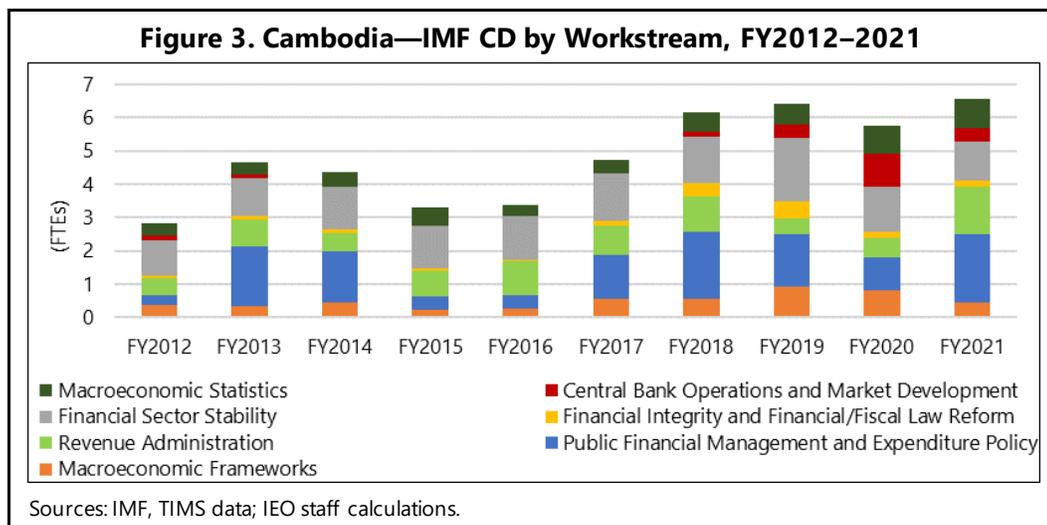
5. Over the review period as a whole, the Fiscal Affairs Department (FAD) and the Monetary and Capital Markets Department (MCM) have been the largest providers of Fund CD to Cambodia. Since 2018, the contributions of the Institute for Capacity Development (ICD) and the Legal Department (LEG) have expanded (Figure 2).



6. Reflecting the need to broaden the revenue base while increasing tax collection, FAD has provided assistance on strengthening tax and customs administration, as well as tax policy. It has also provided considerable assistance on public expenditure management and treasury management, as well as debt management in recent years. MCM has provided a range of

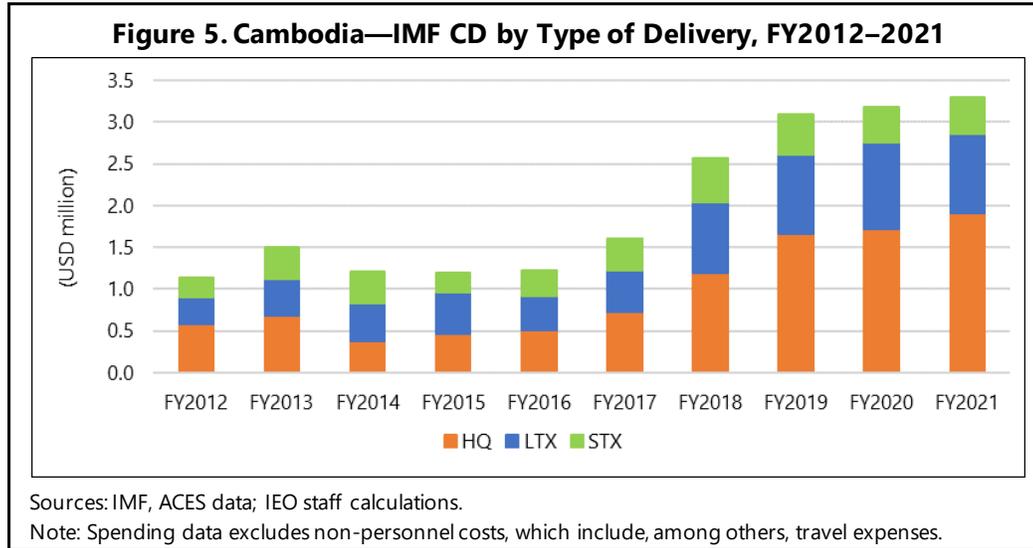
<sup>1</sup> Cambodia, 2019 Article IV Consultation, IMF.

assistance to support Cambodia's efforts to address macro-financial risks as well as bolster capacity in monetary and foreign exchange operations. A Financial Sector Stability Review (FSSR) was conducted in 2019, with follow-up assistance focusing on financial stability analysis and stress testing; other technical assistance (TA) from MCM has covered banking supervision and regulation, liquidity forecasting and interbank development, and establishment of a bank resolution and deposit insurance system (IMF, 2019d). TA from LEG has mainly been in the area of strengthening the anti-money laundering framework, while ICD has provided training to help build capacity in central bank and ministry of finance on macroeconomic analysis and forecasting (see Figures 3 and 4).

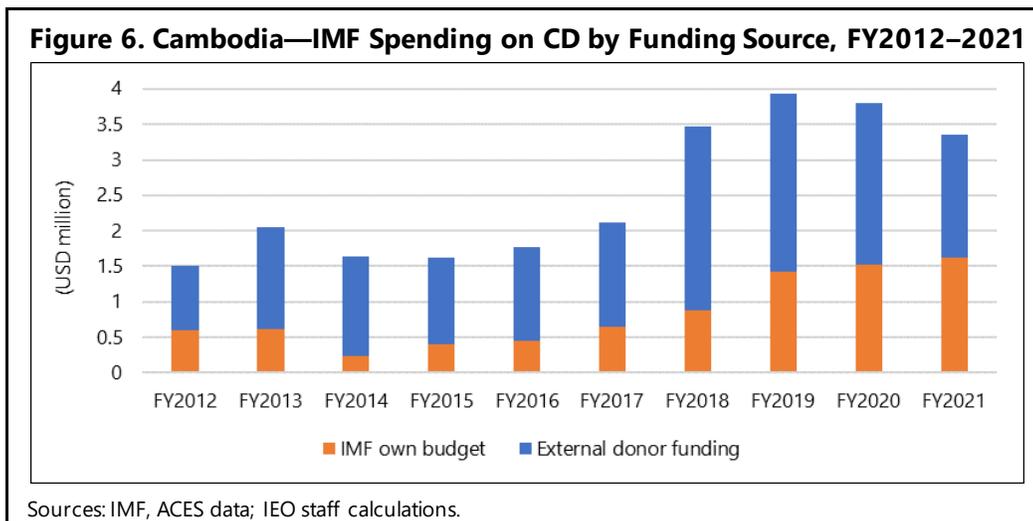


7. IMF departments delivered CD to Cambodia through a mixture of modalities. About 50 percent of the CD has been provided by IMF headquarters (HQ) staff. However, notable in this case has been the support provided by long-term resident experts throughout the past decade, and well as short-term expertise provided by regional advisors located at the Regional Capacity

Development Center (RCDC) in Bangkok (CDOT) (see Figure 5; and Annex I, Table AI.2). The National Bank of Cambodia has benefitted from a series of advisors covering issues related to banking supervision and regulation, and financial stability analysis. An advisor in the area of monetary operations was also provided by MCM in mid-2019. In addition, the Ministry of Economy and Finance was supported by a resident advisor to strengthen macroeconomic forecasting and analysis during 2016–2018.



8. The bulk of IMF CD provided to Cambodia over the period under review has been financed by external donor funds, though the contribution of the IMF's internal budget has risen significantly in recent years (Figure 6), reflecting the FSSR exercise as well as ICD training on macro frameworks. Donor funds from Japan have accounted for almost all of the external financing, with the main exceptions being recent assistance in the areas of financial sector stability and anti-money laundering.



## II. CD ENGAGEMENT

### A. Strategy, Prioritization, and Allocation

9. IMF CD to Cambodia has been well aligned with its key economic challenges and a central component of the institution's engagement with the authorities. CD needs have been wide-ranging and longer-term in nature, covering both policy reforms and efforts to develop capacity. In recent years, the main priorities have included managing macro-financial risks and strengthening the macroeconomic framework, safeguarding fiscal sustainability through reforms to revenue mobilization and better expenditure management, and addressing governance weaknesses and corruption. CD efforts have supported policy reforms and well as the strengthening of institutions and building of technical skills.

10. This CD strategy has for some time been closely integrated with the surveillance work for Cambodia led by the APD country team—even prior to the post-2018 Fund-wide efforts to better integrate CD and surveillance. Planning and monitoring of CD are an integral part of the work of the country team. The strategy is developed in the context of the Article IV process as well as in preparing APD's annual Regional Strategy Notes (RSNs).<sup>2</sup> The country team is in the lead in preparing the strategy—"holding the pen"—but with extensive inputs and iterative discussions with relevant staff of CDDs. Article IV reports have presented a comprehensive picture of recent CD activities along with future main areas of focus in line with strategic priorities. Most recently, the information presented has included a detailed matrix relating surveillance recommendations to TA efforts and key associated results.

11. The CD strategy has involved the close engagement of the Cambodian authorities. Intensive discussions are held during the Article IV mission, meetings with CDDs are held during the Annual and Spring Meetings, and ongoing inputs are provided through the IMF's resident representative in Phnom Penh, who plays a crucial role. Interviews with various officials confirm their involvement in the planning process and indicate their satisfaction with the mix of CD priorities. Reflecting their engagement, staff indicate overall good ownership of the IMF TA and training provided over many years.

12. Notwithstanding these positive features, some issues were raised during the review:

- Ownership could be adversely affected by low capacity of local officials and frequent personnel changes due to rotation practices. Continuous training and hands on follow-up to TA missions and advice were seen to be crucial.

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<sup>2</sup> Stand-alone notes reflecting APD's CD country strategy had also been prepared by country teams in the early part of the review period, but with a view to promoting more efficient work practices, were discontinued as a general practice in APD around 2015. In recent years, country teams have prepared CD matrices which summarize country CD priorities and have been used as inputs for APD RSNs. The matrices are also included as annexes to the RSNs.

- The integration of CD into the work of the country team still depended to some extent on the initiative of the mission chief. In particular, notwithstanding APD's stated intention to incentivize integration through the annual performance review process, performance expectations on CD issues were not consistently defined, nor assessments rigorously applied.
- There seemed to be little relationship between past results and the allocation and prioritization of new CD activities. Proactive engagement by the authorities and availability of funding provided a conducive setting for continued heavy provision of CD. Even in specific instances where ownership was inconsistent or weak, it has proven difficult to slow down or halt CD. In the case of FAD's tax administration project, recommendations for reform to broaden the tax base and increase efficiency were not supported by the revenue administration, which managed to collect increasing revenues using existing methods. In such circumstances FAD sought to scale back its CD in this area, but found it difficult to do so for some time, reflecting continued support for the project by area department staff as well as supportive officials. Ultimately, the IMF provided in 2018 a final diagnosis which could be used for a future reform strategy, but which was not implemented in the short term.
- Notwithstanding the presentations in staff reports, the Executive Director's office sought better information that would provide a comprehensive ongoing picture of activities in their member countries, including of other providers and donors as well, so they could better assist in ensuring effective implementation. At least as far as the IMF's activities are concerned, it is hoped that the Fund's Capacity Development Management and Administration Program (CDMAP) project would help provide significantly better access to information.

## **B. Delivery**

13. The authorities expressed high appreciation for the technical advice and training it has received from the IMF. Moreover, the assistance has generally been well tailored to country circumstances—with institutional and capacity constraints being taken into account to the extent warranted. At the same time, the authorities indicated their satisfaction with follow up and training to assist in the implementation of TA recommendations. They noted in particular the regional training and capacity building through CDOT, for example, in the establishment of a core group of experts in macroeconomic forecasting and analysis drawn from staff in the Ministry of Finance and Economy and the National Bank of Cambodia.

14. CD provided to Cambodia has featured a flexible approach in line with different needs. As seen above, delivery has been effected through an array of modalities—missions from headquarters with IMF specialist staff as well as external short-term experts (STXs), long-term resident advisors, regional advisors located in CDOT, and training in Cambodia and IMF training centers abroad (including from CDOT and the Singapore Regional Training Institute (STI)). Long-

term resident advisors were able to develop deep knowledge and trust and provide continuous hands-on assistance. STXs from HQ and peer agencies brought the latest international expertise to bear. Regional advisors from CDOT could bridge time zone differences and provide nimble and flexible delivery, build close personal relationships, and bring regional knowledge and perspectives.

15. A number of stakeholders pointed to the 2019 FSSR exercise as a flexible, well-tailored and creative approach. The FSSR, a new demand-led TA instrument that provides a baseline diagnostic review and then proposes a detailed roadmap for country TA, covered a key surveillance policy priority for Cambodia. Beginning with a scoping mission that took place in 2018, the authorities were heavily involved from the outset in the design of the Review, thereby enhancing ownership and buy-in. The presence of a long-term advisor (for banking supervision) provided important support, while a range of staff and outside experts brought wide technical and operational knowledge. With funding identified and agreed upfront, experts were readily available to participate in the review.

16. The Cambodian authorities noted that long-term advisors in Asia who can respond to requests on a real-time basis as well as help build capacity by virtue of their on-site presence are a particularly valuable component of CD delivery. However, staff noted that the role of trusted advisor needed to be balanced with the need to: (i) provide the best and sometimes tough advice; and (ii) avoid being regarded as substitute employees, rather than complements located inside Cambodian agencies to help build local capacity.

17. The COVID-19 pandemic period has presented significant difficulties to the IMF's ability to provide CD to Cambodia. With travel frozen and long-term advisors not present at their duty station, the Fund turned to the use of virtual means to deliver CD. Virtual CD has the potential of reaching a large audience and also facilitates availability of a greater number of specialist experts. However, time zone differences have been a difficult issue to navigate, and limited online capacity at officials' homes has constrained delivery in the face of partial or full lockdowns. The authorities consider that there is no substitute for face-to-face interactions but given the need to continue delivery acknowledge that virtual CD is unavoidable in current circumstances. One possible option would be an expanded role for CDOT and/or the STI.

### **C. Partnerships, Coordination, and Dissemination**

18. Interviews held during this review indicate that the IMF coordinates effectively with other CD providers and donors. With the exception of regular annual consultations held in Washington with the primary Japanese donor agency (Japan International Cooperation Agency, or JICA), coordination efforts are mainly informal. And while there is no concerted effort to formulate an overall CD strategy with an agreed division of labor, there are regular efforts to keep all parties informed of each other's activities, to minimize overlaps.

19. Discussions with other providers are centered around the IMF resident representative in Phnom Penh, who maintains ongoing contact with them. One resident representative reported that weekly meetings were held within the international community, including the CD providers. In addition, CDDs meet with other relevant institutions in the context of specific TA projects and/or while on mission in the field. For example, in conducting the 2019 Fund for Financial Support of the Region, MCM staff held discussions with representatives of the Asian Development Bank (ADB), International Finance Commission (IFC), World Bank, and United States Treasury to coordinate TA activities. And FAD teams coordinate in the field with the Bank, Asian Development Bank (ADB), and JICA.

20. Given Japan's role as the pre-eminent source of external donor funds, the IMF staff maintains close contact with relevant Japanese officials. Discussions are held with CDDs as well as the country team to review priority areas, so as to facilitate the appropriate channeling of available funds. Japanese officials are generally satisfied with the level of cooperation, although additional information would be desirable. Specifically, ongoing information on the time horizon of CD projects, and associated progress and outcomes, would be desirable. It is hoped that the IMF's CDMAP project together with committed application of RBM would help in this regard. In addition, access to APD's RSNs and relevant country-specific plans would be help.

21. Duplication and overlaps in CD activities across donors do not appear to be a major problem according to staff; this view is shared by the authorities as well. That said, in some areas such as public financial management (PFM) and new emerging issues (e.g., climate change), some interviewees report a risk of over-reach and unclear division of labor. It would be important to decide how much the Fund should take on in these areas and work closely with other institutions. On a related note, some staff were of the view that the World Bank and other international financial institutions are somewhat reluctant to reveal their CD plans and activities, pointing to the desirability of continued efforts to communicate closely.

22. Turning finally to dissemination, TA reports on Cambodia have in general not been published reflecting the authorities' concerns about the release of sensitive information (see Annex I, Table AI.3). Most recently, however, at least some documents are available on the external IMF website—notably, the report of the 2018 FAD tax reform diagnostic mission that advised on tax administration modernization priorities for 2019–2023.

#### **D. Effectiveness and Impact**

23. It seems clear that IMF CD has made a significant contribution to Cambodia's transition to a market economy and to strengthened macroeconomic management, with TA recommendations implemented on a wide front. There is genuine appreciation of the IMF's technical expertise and CD efforts, strong engagement by the authorities, and ample financing, which all provide a good platform for success. That said, in a number of areas progress has been slow, reflecting low capacity and weak retention of local staff, as well as political constraints and weak ownership of key officials in some cases. All stakeholders interviewed agree that the

process of strengthening and modernizing economic management and the policymaking framework in Cambodia will entail a long-term commitment of capacity and institution building.

24. In the fiscal area, there have been significant successes, but impact has been more limited in others.

- On the revenue side, IMF staff reports that 90 percent of the recommendations under the 2014–2018 Revenue Modernization Strategy were implemented, which helped Cambodia achieve large revenue gains during that period. Improvements in customs administration in line with TA advice were also successfully implemented; one supportive factor was that the customs department officials were also entrusted with external trade facilitation and therefore were fully engaged in modernization efforts. On the other hand, more fundamental reforms to improve efficiency and equity, such as to reduce tax exemptions and preferences, introduce a more modern tax regime, and to reform audit procedures, are yet to be implemented due to resistance by key tax administration officials. The new revenue strategy for 2019–2023 in line with diagnostic work by FAD has been adopted by the authorities. The strategy includes priority recommendations in this area; as of mid-2021, further TA on specific implementation steps awaited definitive engagement by Cambodian officials.
- On the expenditure side, the authorities implemented a number of steps to strengthen expenditure budgeting, reporting, management, and accounting, as well as strengthening public procurement procedures. Overall, the results of the Public Expenditure and Financial Accountability (PEFA) assessment in 2021 suggest that PFM systems in Cambodia have significantly improved in the areas related to fiscal and budget management, though improvements are still needed in areas related to fiscal transparency and reporting, public investment management, medium-term budgeting, expenditure arrears, and payroll. Even in areas that are still weak, some progress is being made. The Open Budget Index (OBI) score for Cambodia has improved from 20 to 32 between 2017 and 2019, indicating progress, though the level remains low.
- Significant success has been achieved in building macro-fiscal analytical capacity, with a host of training provided by CDOT as well as HQ staff. Improvements to macroeconomic and revenue models supported the development of the authorities' medium-term fiscal framework. Also, following the establishment of national "economist program" in 2015, the IMF provided training to a new group of roughly 20 economists each year, thereby supporting the development of a cadre of young economists throughout the government.

25. In the monetary policy and financial sector area, IMF CD has supported improvements to the monetary policy framework, monetary and foreign exchange market operations, and to the macro prudential framework, regulations, and supervisory capacity. A review by MCM in 2019 in

the context of the FSSR found that implementation of past financial sector TA advice was mixed.<sup>3</sup> Most progress was made in banking supervision and regulation, helped by the presence of long-term advisors. But less progress was made other areas, such as stress testing, analytical capacity, and data availability and integrity. The 2019 FSSR received strong engagement of the authorities, who broadly supported its recommendations. The Review provided a roadmap for future TA which the authorities were keen to receive. Since then, the authorities have implemented a host of macro-financial measures and reforms in line with IMF advice, but significant macro-financial vulnerabilities remain.

26. IMF CD has also helped Cambodia address data gaps and improve data quality. Nevertheless, as noted in successive staff reports, deficiencies remain, not least because of resource constraints and capacity weaknesses.<sup>4</sup>

27. The review suggested that there was little systematic use of results to strengthen effectiveness of IMF CD in Cambodia. The RBM tool appears widely used internally by CDDs to set broad objectives and more specific outcomes and milestones; the RBM database contains 28 projects, which in almost all cases have objectives and outcomes defined, though often not rated (see Annex I, Figure AI.1). However, interviews indicate that the authorities were not always involved in its application, contributing to slippage in implementation. Interviews also suggest that past results taken into account in the annual TA planning process.<sup>5</sup> This has led in certain areas to prolonged extensive engagement, reflecting the authorities' proactive and enthusiastic approach to TA requests. The one notable example in revenue administration CD where the TA engagement was at least temporarily wound down entailed considerable internal debate, [as well as discussion with the authorities].

### III. OVERALL ASSESSMENT

28. Cambodia has been a very heavy user of IMF CD over the years. The CD has been well-integrated with IMF surveillance and consistent with the needs of the country, and ownership has generally been high with the authorities heavily engaged and appreciative of the Fund's expertise. In recognition of the institutional and skills shortages, hands-on assistance and training provided by long-term resident advisors, regional advisors, and experts from HQ has been an important component of IMF CD. The success of IMF CD in Cambodia has been facilitated by the strong efforts of successive resident representatives. The contribution of the IMF to Cambodia's transition and development process has also been recognized by the Japanese authorities, who have continued to provide considerable donor assistance.

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<sup>3</sup> This was as reported in IMF (2019d).

<sup>4</sup> See, for example, Cambodia, 2019 Article IV Consultation, IMF.

<sup>5</sup> It is striking that the comprehensive 2019 FSSR report notes that past implementation of TA recommendations has been mixed yet does not discuss ways to mitigate risks or strengthen effectiveness in presenting its forward-looking TA roadmap.

29. Notwithstanding the overall positive assessment, the effectiveness of IMF CD could be enhanced in a few respects. Although CD prioritization going forward has been in line with key challenges identified in the surveillance process, medium-term planning does not appear to be rigorously informed by results and implementation of previous TA recommendations. Country strategies presented in Article IV reports as well as APD Regional Strategy notes take little account of results in deciding the optimal allocation of available resources, suggesting that use of RBM remains a work in progress.<sup>6</sup> Long-term engagement has continued in several areas despite poor implementation, and the experience of FAD CD in the area of tax administration reform illustrates the difficulty of scaling back delivery in the event of incomplete stakeholder ownership. A periodic in-depth examination of results—say in the context of establishing a medium-term country engagement strategy—could be helpful in strengthening traction.

30. Given the importance of broad ownership, the consistent agreement with the authorities of early and ongoing milestones which are their responsibility to implement would also help ensure successful demand-driven CD. Despite the internal use of RBM by staff in CDDs, associated log frames and milestones do not appear to be regularly discussed with recipient agencies.

31. Such additional rigor in the prioritization and planning process would also strengthen further the impact of long-term advisors. The placement of a resident expert in the field represents a large investment of resources. Such a decision should be made taking explicit account of prior results and likely future success of capacity building efforts. The authorities' engagement would be strengthened by ensuring their participation in the selection process for any new long-term expert (LTX).

32. The availability of better tools than in the past would help the country teams better manage the planning and governance of IMF CD for Cambodia. In this regard, the successful implementation of the Fund's CDMAP project would seem critical. Better information would also help the Executive Director's office to support implementation.

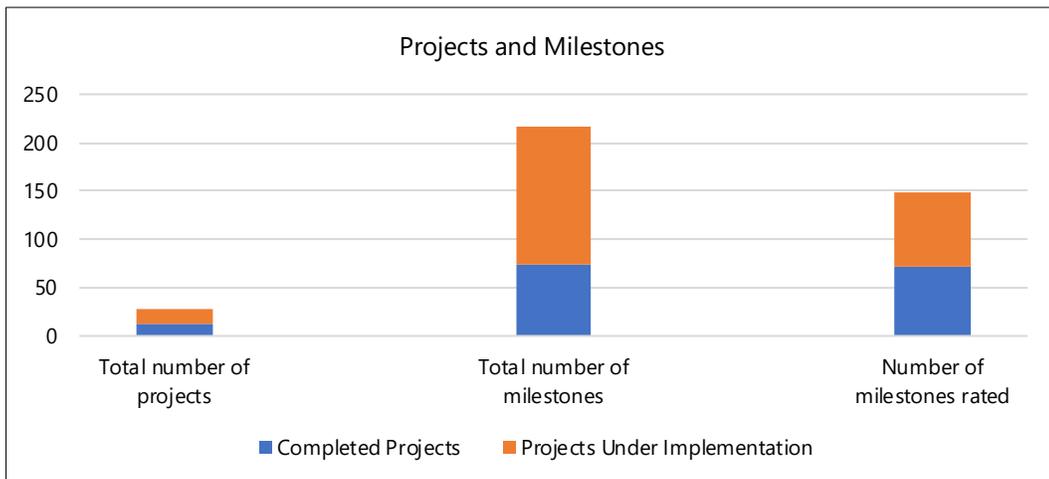
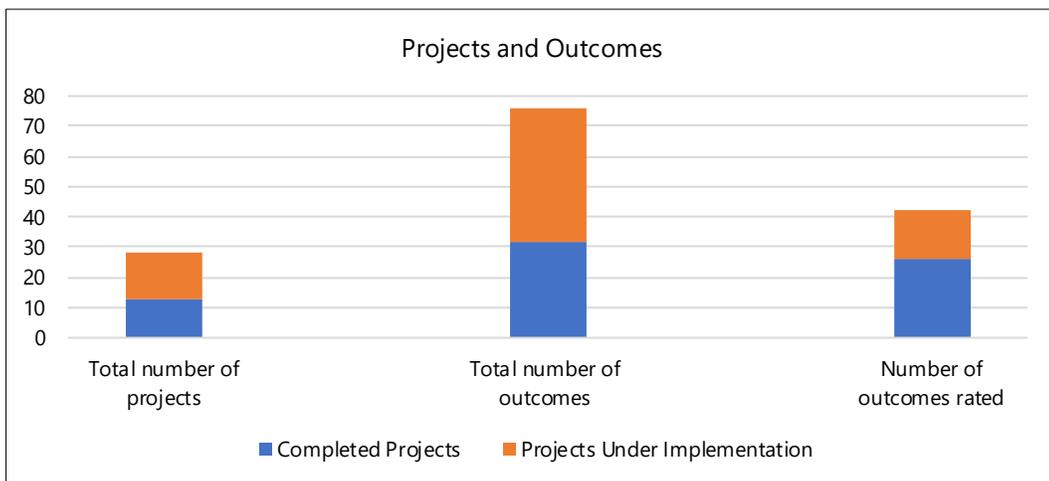
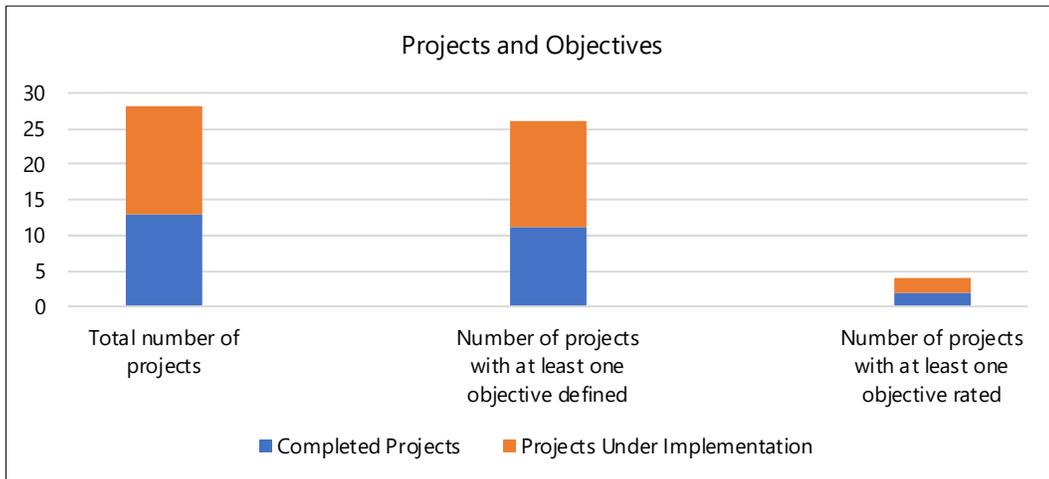
33. Finally, in view of the positive role played by regional advisors, and given the likely persistent impact of COVID on mission travel, thought should be given to how best to maximize the role of CDOT and the regional training center in Singapore. An expansion of funding sources could help in this regard. At the same time, the desirability of deploying international expertise centered at headquarters and the need to ensure sufficient resources at headquarters to provide backstopping and quality control should be recognized.

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<sup>6</sup> The notes reflecting APD's CD country strategy produced up until 2015 did contain a discussion of previous implementation of TA recommendations, with a quantitative scoring, but such assessments are no longer a feature of the CSNs introduced Fund-wide in 2018.

**ANNEX I. CD ACTIVITIES FOR CAMBODIA**

**Figure AI.1. Cambodia—Results-Based Management Data on Projects, Objectives, Outcomes, and Milestones**



Sources: IMF, RBM data; IEO staff calculations.

**Table AI.1. Cambodia—Number of Missions, 2012–2020**

Year	FAD	ICD	LEG	MCM	RES	STA	Others	Total
2012	10	0	0	3	0	5	0	18
2013	19	0	0	2	0	4	1	26
2014	14	0	0	5	0	2	0	21
2015	19	0	0	1	0	5	0	25
2016	17	0	0	2	0	3	5	27
2017	21	0	2	6	0	3	6	38
2018	28	0	7	5	0	3	8	51
2019	21	0	7	24	0	2	19	73
2020	19	1	3	9	0	7	12	51
Total	168	1	19	57	0	34	51	330

Sources: IMF, TIMS data; IEO staff calculations.

**Table AI.2. Cambodia—Resident Advisors, 2012–2021**

Host Institution	CDD	CD Topic/Workstream	Start Date	End Date
Central Bank	MCM	General Advisor to the National Bank of Cambodia (Year 1)	10/6/2011	10/5/2012
Ministry of Finance	FAD	Accounting	5/25/2012	5/24/2013
Central Bank	MCM	General Advisor to the National Bank of Cambodia (2 <sup>nd</sup> Year Extension)	10/6/2012	10/5/2013
Ministry of Finance	FAD	Extension of Accounting Resident Advisor (Two Month Extension Waiting for JSA Approval)	5/25/2013	7/24/2013
Ministry of Finance	FAD	Extension of Accounting Resident Advisor	7/25/2013	4/30/2014
Central Bank	MCM	General Advisor to the National Bank of Cambodia (3 <sup>rd</sup> Year Extension)	10/6/2013	10/5/2014
Central Bank	MCM	General Advisor to the National Bank of Cambodia (4 <sup>th</sup> Year Extension)	10/6/2014	1/5/2015
Central Bank	MCM	Banking Supervision Resident Advisor (Year 1)	12/15/2014	12/14/2015
Central Bank	MCM	Banking Supervision Resident Advisor (2 <sup>nd</sup> Year Extension)	12/15/2015	12/14/2016
Ministry of Finance	FAD	Macro-Fiscal Resident Advisor	11/30/2016	11/29/2017
Central Bank	MCM	Bank Supervision and Regulation Advisor (3 <sup>rd</sup> Year Extension)	12/15/2016	12/14/2017
Ministry of Finance	FAD	Extension of Macro-Fiscal Resident Advisor	11/30/2017	11/29/2018
Central Bank	MCM	Banking Supervision Advisor (3-Month Extension—Year 4)	12/15/2017	3/14/2018
Central Bank	MCM	Financial Stability Advisor (Year 1)	7/14/2018	7/13/2019
Ministry of Finance	FAD	Extension of Macro-Fiscal Resident Advisor	11/30/2018	12/8/2018
Central Bank	MCM	Banking Supervision Resident Advisor (Year 1)	12/1/2018	11/30/2019
Central Bank	MCM	Monetary Operations Resident Advisor (Year 1)	7/29/2019	7/28/2020
Central Bank	MCM	Banking Supervision Resident Advisor (2 <sup>nd</sup> Year Extension)	12/1/2019	11/30/2021
Ministry of Finance	FAD	PFM	5/11/2020	5/10/2021
Ministry of Finance	FAD	Resident Regional Customs Modernization Advisor	8/10/2020	8/9/2021

Sources: IMF, Fiscal Affairs Department and Monetary and Capital Markets Department.

**Table AI.3. Cambodia—List of TA Reports, 2012–2020**

	FAD	MCM	STA	LEG	Total	Of which		
						Available Within IMF	Available but Confidential	Published
2012	4	0	3	0	7	5	0	0
2013	3	3	2	0	8	5	0	0
2014	1	2	3	0	6	2	2	0
2015	3	1	2	0	6	4	0	0
2016	5	2	1	0	8	7	0	0
2017	1	2	1	0	4	2	0	0
2018	3	4	1	0	8	1	0	1
2019	1	3	4	0	8	3	0	0
2020	2	1	2	0	5	5	0	0
Total	23	18	19	0	60	34	2	1

Source: IMF, Institutional Repository.



# **PEOPLE'S REPUBLIC OF CHINA**

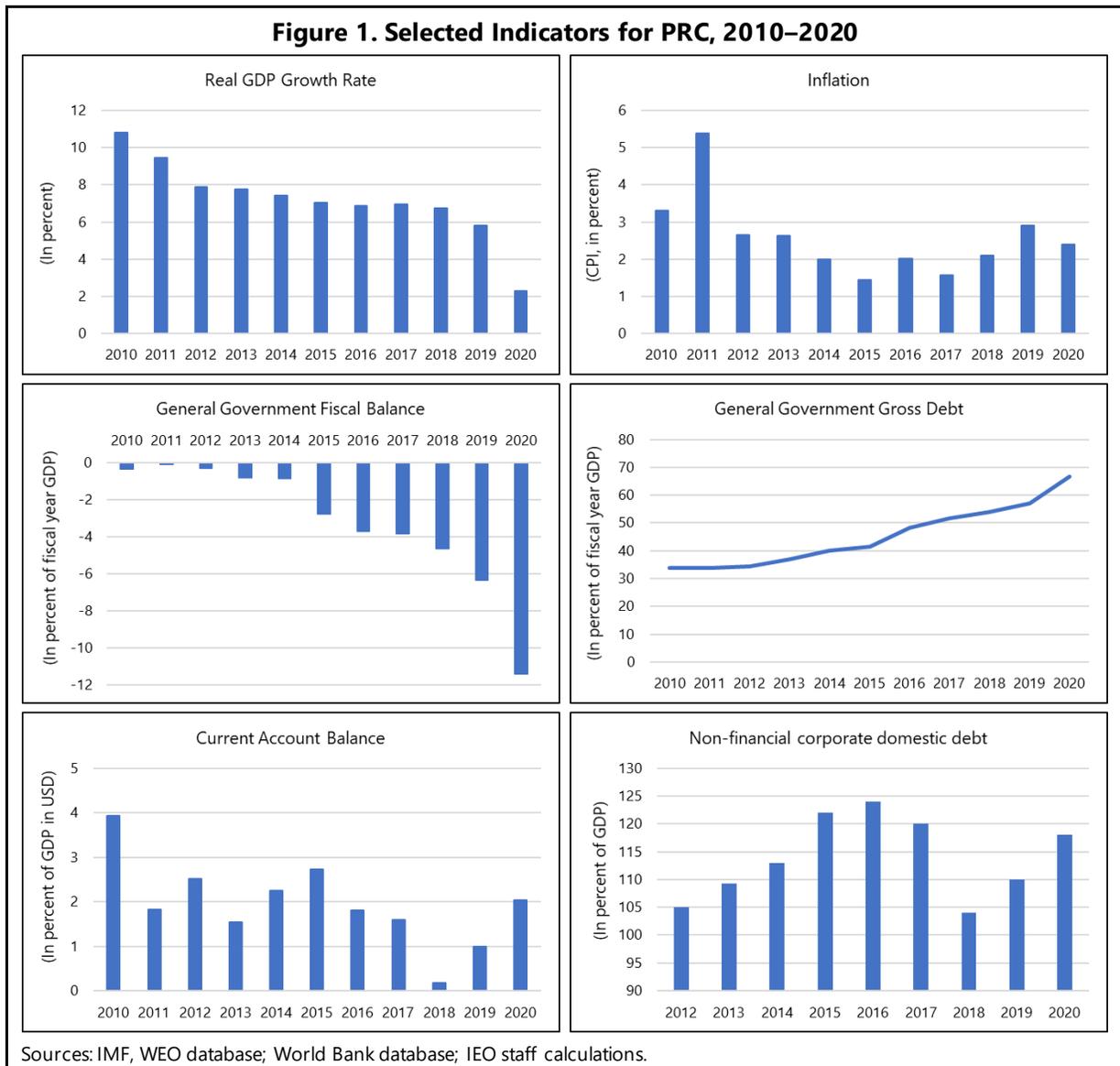
**CHRISTOPHER LEGG\***

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\* Consultant, Independent Evaluation Office of the IMF.

## I. INTRODUCTION AND COUNTRY OVERVIEW

1. The People's Republic of China (PRC) is the largest systemically important economy to which the IMF continues to provide significant levels of CD. It is also the Fund's third largest member in terms of quotas, and increasingly a potential development partner. The Fund's engagement with the PRC is therefore central to its mandate to promote international monetary cooperation and stability.
2. Over the review period, annual growth rates have steadily declined from earlier double-digit levels along with moderation of the current account surplus—and underlying savings-investment imbalance—notwithstanding some recent re-widening. Increasing fiscal deficits have been associated with higher domestic debt levels in both the general government and corporate sectors (see Figure 1).



3. The authorities' macroeconomic policy focus since 2012 has been on managing vulnerabilities associated with an unsustainable reliance on investment, credit and fiscal stimulus and rebalancing towards domestic demand and consumption. Consistent with aspirations to become a prosperous modern socialist country,<sup>1, 2</sup> longer-term economic objectives involve improving capital allocation, innovation and productivity. These challenges have recently been compounded by external geo-political tensions and the COVID-19 shock.

4. Over this period, in addition to the near-term challenges around macroeconomic policy settings, Fund surveillance, including Financial Sector Assessment Programs (FSAPs) in 2011 and 2017, has consistently highlighted a number of key longer-term issues associated with the authorities' declared objective of enhancing the role of markets in the domestic economy:

- The desirability of welfare, labor market and related (including tax) reforms to address inequality and enhance inclusive growth;
- Enhancements to fiscal policy frameworks and statistics to facilitate an integrated medium-term approach to fiscal policy's macroeconomic role and impact;
- State-owned Enterprise and other reforms to enhance competition and efficient capital allocation;
- The development of monetary policy and regulatory frameworks, including macro-prudential policy, in line with the requirements of an efficient market-based financial system; and
- The scope for further gradual capital account liberalization.

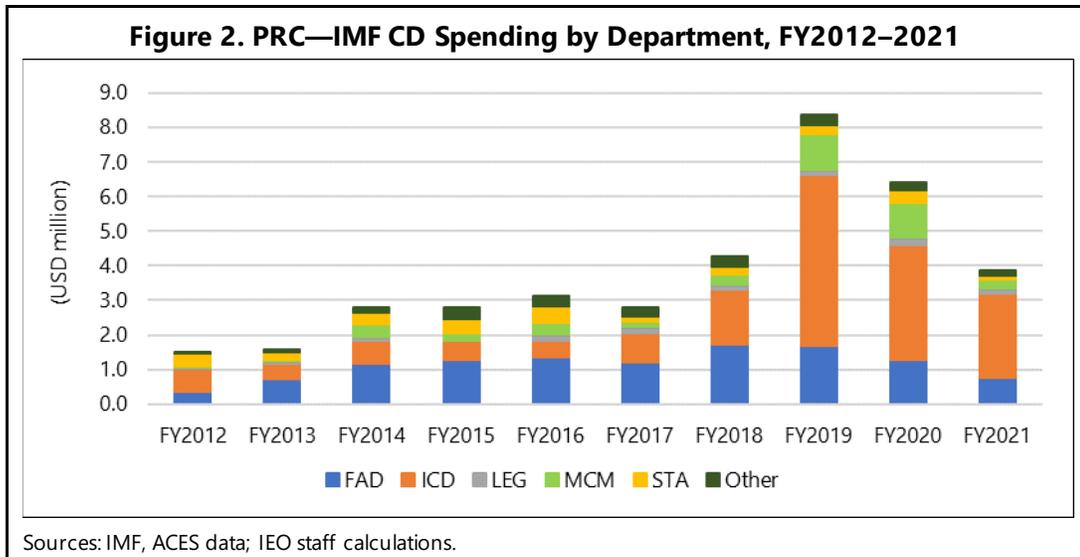
5. The PRC has robust domestic institutions. However, in a system that combines a strong central administration alongside considerable decentralization, there is pressure to adjust to both the increased role of markets and the country's expanding global economic integration. Understanding of market-based policy frameworks, and the need to accommodate volatility, is not deeply embedded in PRC institutional culture.

6. In this context, the IMF's CD activities with the PRC grew steadily between 2012 and 2018 (Figure 2). By FY2018, PRC was the fifth largest recipient of CD amongst countries covered by the Fund's Asia and Pacific Department (APD), and the only country in APD's top ten CD recipients not a low middle-income country.

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<sup>1</sup> The second of President Xi Jinping's two centenary targets announced following the 18<sup>th</sup> National Congress of the Communist Party of China in 2012; the first, to become a "moderately prosperous society" by the centenary of the creation of the Chinese Communist Party in 2021, was achieved by doubling 2010 GDP per capita.

<sup>2</sup> As of 2019, China's gross national income per capita was US\$11,553 compared to the upper threshold of the World Bank's middle-income country classification of US\$12,695.



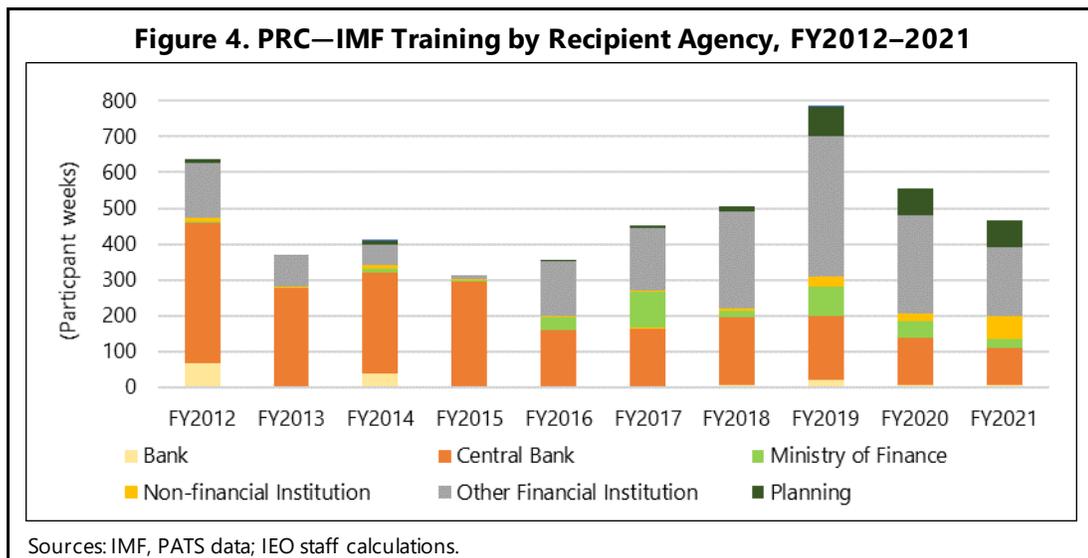
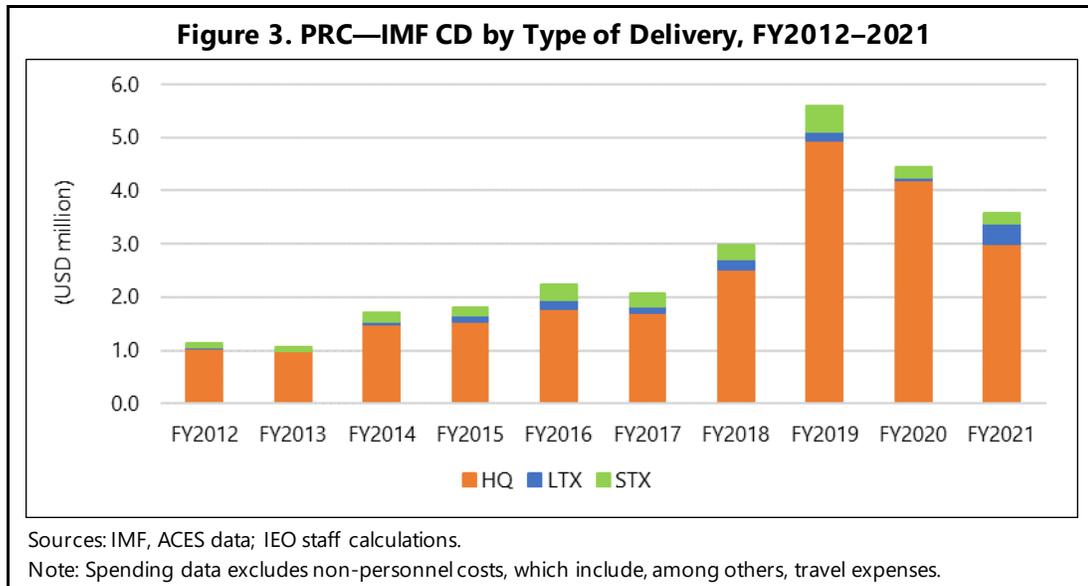
7. In response to PRC’s increasing demand for Fund CD and interest in adopting a more medium-term approach,<sup>3</sup> and building on a model first formalized with PRC’s State Administration of Taxation (SAT), Memorandums (and Letters) of Understanding (MoUs/LoUs) have been progressively agreed to facilitate the development and implementation of joint work programs.<sup>4</sup> These arrangements recognize the siloed nature of China’s system and the need for governance architecture which underpins individual institutional contact while respecting the primacy of the Fund’s relationship with the People’s Bank of China (PBoC). In addition to a longstanding partnership with SAT, new areas of activity have included: follow-up support on recommendations emerging from the 2011 and 2017 FSAPs including the development of macroprudential policy frameworks and tools; budget and accounting reforms focused on enhancing the transparency of fiscal vulnerabilities, especially at the provincial level; strengthening macro fiscal frameworks and capacities; and broadening understanding of debt sustainability issues. China’s 2015 adoption of the Special Data Dissemination Standard (SDDS) has underpinned engagement on statistics.

8. Core modes of delivery have been mostly HQ missions, sometimes supported by STX (Figure 3 and Annex I). In addition, a Senior Financial Sector TA Advisor was appointed to the PBoC between 2018 and 2020, and there has been extensive use of workshops and seminars to build understanding across institutions and levels of government. Increasing demand for tailored training activities for both Chinese officials and those of other countries including Belt and Road

<sup>3</sup> This was reported by a high-level mission in 2016, involving APD, FAD, MCM, and STA which met with counterparts from PBoC, China Banking Regulatory Commission (CBRC), China Securities Regulatory Commission (CSRC), the State Administration of Foreign Exchange (SAFE); the MoF; the SAT, the NBS and the National Development and Reform Commission (NDRC).

<sup>4</sup> In addition to the SAT, with which the first MoU was established in 2013 and most recently renewed in 2019, MoUs/LOUs have now been agreed with the Ministry of Finance (MoF, 2015 and 2019), China Securities Regulatory Commission (CSRC, 2016), National Bureau of Statistics (NBS 2017), PBoC (2017) and China Banking and Insurance Regulatory Commission (CBIRC, 2019).

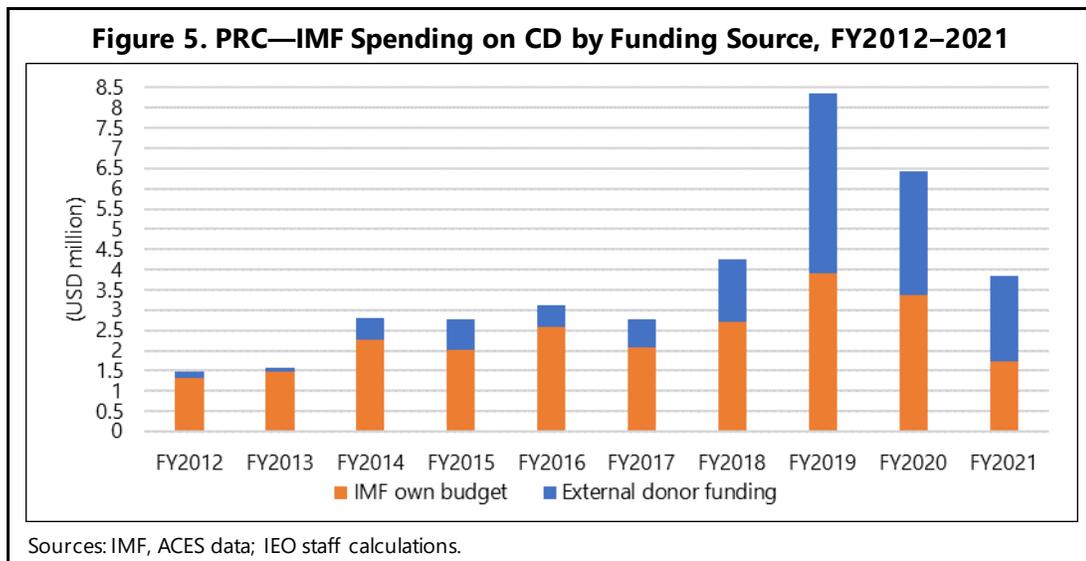
Initiative (BRI) participants, saw the 2017 launch of the China-IMF Capacity Development Center (CICDC), focused on supporting in-country training activities, and a significant expansion on the earlier China Training Program with strengthened ownership by the authorities<sup>5</sup> (Figure 4).



9. At the same time, other sources of CD external assistance to PRC have been minimal as other development partners have reduced engagement in line with the PRC's high middle-income status or, as in the case of the World Bank, withdrawn from CD provision given the authorities' reluctance to borrow for CD.

<sup>5</sup> The CICDC was established in May 2017, with a five-year budget of US\$27.2 million fully funded by the PBoC, a Center Coordinator appointed by the IMF and training to be provided by Fund staff. Its operations are overseen by a Steering Committee consisting of senior representatives of the PBoC and the Fund (ICD and APD).

10. The Fund’s willingness to draw disproportionately on IMF01 resources for its CD to PRC, alongside targeted co-financing arrangements with the authorities on specific projects and activities, has therefore been important. Over the review period, the predominant focus of joint funding arrangements has been a series of three multi-year CD projects agreed with SAT on tax reform and administration, with a cumulative commitment by the authorities of US\$5.6 million. More recently, the authorities’ willingness to supplement Fund resources is evident in the PBoC’s agreement to fully fund the CICDC (Figure 5).



## II. CD ENGAGEMENT

11. Over the review period, the Fund’s CD to the PRC has sought to respond to a marked increase in the authorities’ interest in market-based policy frameworks and the lessons from other country experience, while confronting the challenge of how best to establish effective sustained partnerships within China’s sui generis system, with a view to optimizing the benefits of this engagement over the long term.

### A. Strategy, Prioritization, and Allocation

12. The CD relationship with PRC has been seen by the Fund as an integral—and evolving—part of a broader engagement strategy which acknowledges the PRC’s growing importance to the global economy and to the Fund’s mandate. The PRC’s need to modernize its institutional frameworks, the increasing potential for significant global spillovers (and spillbacks) associated with developments in the PRC and its growing role as a development partner are all highlighted in both the Fund’s 2017–2018 Capacity Building Strategy Note and 2020 Country Strategy Note (CSN) for PRC as justification for continuing and flexible engagement, notwithstanding uncertainties around potential traction.

13. Notable elements in the Fund’s approach have been:

- Recognition of the importance of building personal relationships of trust at all levels, reflected in the active engagement of the Managing Director and Deputy Managing Director at the highest levels of the Chinese system and efforts to echo this through all levels of engagement, investing where possible in continuity and institutional knowledge—in particular in the position of resident representative which has played a pivotal role in shaping and managing the CD relationship;
- The development of an architecture for the CD relationship—built around the system of MoUs/LoUs—intended to facilitate annual consultations and related processes on agreed priorities and workplans, including a biennial meeting with all counterparts;
- The establishment of an internal Fund coordination process, anchored by an annual meeting convened by APD and incorporating ICD and the CDDs, usually held between the Article IV Mission and the Board discussion, which appears to have been broadly effective in ensuring alignment with surveillance priorities; and
- A clear commitment to being nimble and innovative in responding to the authorities’ requests in a demand-driven relationship.

14. Examples of such nimble and innovative responses include: FAD’s CD on government financial reporting over the period 2014–2018, in response to the priority expressed at the highest level of the authorities to improve the management of fiscal and quasi-fiscal vulnerabilities, especially at the provincial level; the timely appointment<sup>6</sup> (reportedly agreed at the highest levels of the Fund and PRC) of the Senior Financial Sector TA Adviser to play a very hands-on role building trust and influence within the People’s Bank as part of a deepening dialogue on financial sector risks following the PRC’s 2017 FSAP and concerns within the authorities regarding a potential “Minsky moment;”<sup>7</sup> engagement on debt sustainability issues following an exchange with PRC officials in the margins of the Paris Club, and the subsequent development of a modified debt sustainability training course targeted jointly at Chinese creditors and third-party sovereign borrowers, since delivered several times (which reportedly reflected groundwork done by the resident representative to highlight potential balance sheet risks associated with China’s often uncoordinated and unmonitored overseas lending and took advantage of the flexibility offered by the CICDC to move quickly, outside of established arrangements with the World Bank on these issues); and FAD efforts to support former Finance

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<sup>6</sup> In July 2017, the establishment of the State Council Financial Stability and Development Committee was announced, designed to strengthen a coordinated focus on financial stability issues among the PBoC and the three regulatory Commissions, (for banking, insurance, and securities), chaired by a Vice Premier and supported by a secretariat within the PBoC.

<sup>7</sup> In the margins of the 19<sup>th</sup> Communist Party Congress in late 2017, outgoing PBoC Governor Zhou Xiaochuan publicly highlighted the risks of a “Minsky Moment”—a sudden collapse in asset prices after a period of unsustainable growth driven by excessive pro-cyclical factors and sparked by debt or currency pressures.

Minister Lou Jiwei's initiative to create a macro-fiscal policy department within the Ministry of Finance (MoF).

15. The PBoC-funded CICDC is an important development in the overall CD relationship, facilitating joint ownership of efforts to address the increasing demand for customized training. Incorporating the PBoC and senior representation from ICD and APD (including the resident representative), the Center's Steering Committee appears to be an effective joint governance mechanism, with the PBoC coordinating and channeling counterparty agencies' requests for training. In particular, the Steering Committee appears to be effective in promoting a shared understanding of overarching priorities and the role the CICDC can play within that, consistent with the Fund's overarching commitment to aligning CD with identified policy needs.<sup>8</sup>

16. There is no evidence of CD prioritization being driven by funding constraints. The Fund's willingness to use IMF01 revenues to support an important relationship and ensure responsiveness to country demand is clear. Equally, progress has been made on developing joint funding arrangements which reflect the value the authorities see in assistance on specific issues and/or delivery modes (such as training). Despite some reported difficulties settling cost sharing arrangements under some MoUs/LoUs, prioritization within broadly defined areas of focus has been largely shaped by the authorities' interest in engaging on specific issues, and the extent of the Fund's institutional flexibility to respond.

17. The Fund's overall approach implicitly acknowledges that the authorities will set the pace at which CD is digested and its potential applicability weighed and internalized, with limited external visibility of relevant internal processes, while approaches to implementation are often cautious and rely on targeted piloting in a complex multilayered system. This lack of clarity over potential traction makes it difficult to judge the optimal level of CD investment. However, to date the balance struck seems appropriate, given the breadth and complexity of the transition China is seeking to manage and what is at stake for the global economy and the Fund's mandate.

18. The intensity of engagement with different agencies varies significantly. The PBoC is active both as the primary custodian of the Fund relationship and as a CD recipient, while the SAT remains actively engaged in its joint workplan on revenue administration and policy reform. In contrast, the National Bureau of Statistics (NBS) has shown little interest over recent years in engaging on statistics CD. The MoU with the CBIRC was only finalized in November 2019 and joint work program is yet to be agreed, while successive joint work programs with the China Securities Regulatory Commission (CSRC) consist of annual seminars on agreed topics. MoF engagement appears patchy, while COVID appears to have disrupted some of the mechanisms

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<sup>8</sup> The 2020 Steering Committee minutes note that the authorities identify the following four broad areas as priorities for the CICDC: (i) macroeconomic analysis and management; (ii) financial sector surveillance and policies; (iii) debt issues; and (iv) economic integration and the BRI. All are fully consistent with the Fund's Country CD Strategy and with the consistent themes in the surveillance discussion over the review period.

for ensuring buy-in across counterparts, such as the biennial collective meeting. And the National Development and Reform Commission (NDRC), a key PRC player in macroeconomic policy, was a notable omission from the list of formal counterparts.<sup>9</sup>

19. This underlines the importance of the Fund continuing to invest in a shared understanding of its strategic approach across relevant Departments. Not all Fund staff interviewed by the IEO demonstrated a clear awareness of the Fund's strategy. The annual internal coordination meeting was deferred in 2020, as COVID took precedence over business as usual. And Fund staff turnover has eroded institutional memory in some areas. More fundamentally, the Fund needs to continue to work hard to preserve the long-term relationships, including at the highest level, that are a cornerstone of the strategy.

## **B. Delivery**

20. Insights regarding CD delivery for the PRC can be drawn from the experience on three fronts: the operation of the institutional architecture of MoUs/LoUs and associated processes established to shape and facilitate delivery of CD to relevant counterpart institutions; the focus on training and in particular the contribution made by the establishment of the CICDC; and the appointment of a Senior Financial Sector TA Adviser to the PBoC.

### **MoUs/LoUs**

21. The first of these implicitly acknowledges the challenges involved in engaging a system which is highly siloed and more comfortable with formal structures. It has also offered a mechanism to engage on joint funding arrangements, although difficulties in agreeing on how to operationalize this principle appear to have complicated efforts to develop and implement work plans with some counterparts.

22. The longest standing relationship, that with the SAT, arguably provides a model for the others. Agreement on the 2013 LoU responded to the authorities' request to build on a history of engagement on revenue issues over several decades, with significant continuity of personnel on both sides. It established a joint SAT/IMF three-year funding arrangement for a detailed work program involving HQ led missions, HQ supported experts and training, focusing on revenue analysis, audit and compliance issues and associated training, and international tax issues. Two subsequent multi-year work programs have been agreed, spanning 2016–2021 and covering a wide range of both revenue administration and policy issues. Notable features have included incorporation of external (non-IMF) expertise on the Chinese tax system and context; extensive efforts to ensure ownership of the work program at all levels in the Chinese system, including an initial high-level workshop; extensive outreach to and engagement with provincial SAT officials; and intensive efforts to ensure the system's buy-in to the resulting conclusions and recommendations. Collaborative preparation of lengthy reports, widely disseminated within the

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<sup>9</sup> However, staff note that in 2021 CICDC delivered training courses for NDRC officials.

Chinese system, is seen as central to this process. SAT officials have highlighted the value added by the Fund in helping localize the recommendations for implementation.

23. The experience under the other MoUs/LoUs has been more mixed.

- Early work on Public Financial Management (PFM) issues (including a Treasury Single Account (TSA), government financial reporting reform, the authorities' interest in accrual accounting (with a focus on provincial government balance sheets), international experience with medium-term expenditure frameworks with the MoF) largely pre-dated the 2015 MoU. Formal agreement on a workplan under the latter appears to have never been finalized and there has been little progress on operationalizing its 2019 successor. Disruptions associated with the pandemic are no doubt part of the recent story. However, there are also concerns that the MoU may have added layers of internal MoF process (with the Fund now communicating through the MoF's international department rather than directly with the relevant department, such as the TSA work with the MoF's Treasury). Although less of a practical problem in a virtual delivery world, staff also noted difficulties reaching agreement on operationalizing the 50:50 cost split envisaged under the MoU. While the authorities' motivation for some requests has been clear, for example, provincial balance sheets, on others such as (performance-based budgeting, it has been less obvious. The authorities' response to a 2019 high level FAD workshop on macro-fiscal policy was seen by staff as implying continued interest in this and a follow-up virtual mission is anticipated this year.
- Settling the practicalities of joint funding arrangements under the 2016 MoU with the CSRC has reportedly proven difficult. Moreover, the pandemic has disrupted subsequent planning and, according to CSRC officials, the regular communication envisaged under the MoU. They attributed this to distractions and staff movements on both sides.
- Officials noted that the direct contact with MCM, envisaged under the 2019 CBIRC MoU but "lost" at the start of the pandemic, should be reactivated in due course to progress work on the envisaged work program.
- The 2017 MoU with the NBS has relatively general high level ambitions—improving national accounts methodologies—while identifying selective areas for possible cooperation. However, STA did not identify NBS as a primary PRC counterpart, and only 4 out of 30 STA missions to PRC since 2011 have occurred since 2017, with only 1 of these on the national accounts. Rather, STA's limited CD to PRC has been primarily driven by the latter's 2014 decision to subscribe to the SDDS, with engagement largely on monetary and financial statistics and the external sector.

## Training

24. China's strong learning culture and demand for training is evident across the full range of CD delivery. The FAD/SAT experience of extensive outreach exposing large numbers of officials to the material is broadly echoed across other activities. The sole focus of the 2017 PBoC LoU is the 5-year funding agreement supporting Fund CD and in particular the creation of the CICDC. Aiming to deliver some 20 courses/workshops annually, compared to between 5–12 courses a year through the earlier jointly-funded China Training Program (CTP), the Center provides enhanced scope to tailor courses better to Chinese circumstances.<sup>10</sup> With a third intended to be open to participants from other (primarily BRI participating) countries and up to three courses held in other countries each year, it acknowledges the PRC's expanding global footprint, an important element for both the authorities and the Fund's country CD strategy. Courses/workshops offered have broadly fallen within four broad themes agreed by the steering committee: macroeconomic analysis and management, financial sector surveillance and policy, debt issues, and regional economic integration. In keeping with limited CD engagement with the NBS, there have been no statistics courses delivered to date,<sup>11</sup> notwithstanding the fact that the number of PRC participants in STA training courses more generally were more than double that for any other APD member since 2011.

25. The development and delivery of a customized course on debt sustainability analysis underscores the potential strengths of the CICDC. It offered the means to tailor the established debt sustainability training to the interests of both Chinese creditors and third country borrowers, to do so quickly, and to deliver it efficiently. Moreover, to paraphrase a staff member involved in this process, it was easier to attract participants to a joint China/Fund "learning center" than to a Fund TA workshop.

## Senior Financial Sector TA Adviser to PBoC

26. The experience of the Senior Financial Sector TA Advisor appointed to the PBoC highlights the potential value of the trusted adviser. Facilitated by the strength of high-level relationships with the authorities, the appointment provided unprecedented access to senior officials at a crucial juncture of operationalizing the newly established State Committee on Financial Stability and Development. Careful navigation of the gray area between CD and policy advice was required, alongside the need to build trust and respect confidentiality in relations with senior counterparts.

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<sup>10</sup> In practice, the onset of the pandemic during its start-up phase has seen initial levels of activity fall short of these aspirations, with between 13–15 courses/workshops in each of FY2020 and FY2021, although the ratio of China only/third country invited activities has been broadly preserved, and 2–3 courses each year delivered through one of the Fund's other regional training centers.

<sup>11</sup> Recent proposals for statistical training courses to be hosted by CICDC have not proceeded, reflecting a preference for in-person training.

## **The COVID-19 Pandemic**

27. The pandemic has inevitably disrupted the start-up of the CICDC training program, with a shift to virtual delivery of training involving a degree of adaptation and innovation distinguishing between elements requiring synchronous delivery and those that can be done in nonsynchronous sessions. Limitations on travel have constrained the ability to bring participants together and courses have been shortened to accommodate the competing pressures on participants remaining at their workplace. While all interlocutors acknowledge the potential enhanced use of virtual delivery tools beyond the end of the pandemic, the strengths of face-to-face delivery and participation are judged hard to replicate.

28. Perhaps more importantly, the pandemic appears to have undermined the sustained investment in relationships needed to underpin the effectiveness of the MoU/LoU architecture built over recent years. This would seem to be a particular risk in the case of the less well developed CDD relationships with some counterpart agencies.

### **C. Partnerships, Coordination, and Dissemination**

29. PRC's external partners face an idiosyncratic operating environment. This includes strong but highly siloed institutions, tight management of access, a propensity to deal separately with individual external partners and often requesting advice on the same topic from multiple sources to be weighed and compared, and the general opaqueness of internal processes. The review period has also seen a steady decline in the number of external donors active in CD to the PRC. Consequently, the coordination challenge is largely internalized by the authorities.

30. The World Bank remains the Fund's primary partner on PRC operations, and there appears to have been active and regular engagement both across 19<sup>th</sup> street in DC and in Beijing. However, this has become less relevant on CD as the authorities' reluctance to borrow for CD has meant that the Bank is effectively no longer a provider. Moreover, the authorities' strong preference for preserving the confidentiality of CD advice necessarily limits information sharing with the Bank and other donors, beyond informal exchanges of a general nature. Respecting the authorities' preference is rightly seen as central to preserving the Fund's standing with Chinese counterparts.

31. Nonetheless, all interlocutors emphasized the important role played by the Fund's resident representative, and the benefits to the Fund of having invested over the last decade in continuity and local knowledge in this position. The resident representative plays an important role in maintaining informal contact with other donors on the ground, in particular the Bank's Beijing based Country Director, and arguably more importantly, in sustaining and deepening relationships of trust with key counterparts, in recent years alongside the CICDC Coordinator.

32. Fund staff interviewed generally had little expectation that the authorities would consent to the public dissemination of CD reports or related materials and saw little point in using

relationship capital to argue in favor of public release.<sup>12</sup> However, as demonstrated by the practices developed with the SAT and echoed in other areas such as PFM, Fund CD reports are disseminated and discussed widely within the Chinese government system, including at provincial level where the subject material is relevant. This would seem to be an important part of the process of generating buy-in and fostering implementation.

#### **D. Effectiveness and Impact**

33. The Fund's country CD strategy for PRC clearly has a number of multilayered objectives: to complement the policy dialogue by broadening and deepening understanding of market based policy and regulatory systems; the provision of support for tangible outputs and outcomes that support market mechanisms, building resilience and accommodating volatility; helping to shape the PRC's impact on regional and global outcomes as its international presence increases; and strengthening a relationship of trust in the context of the PRC's increasing weight as a member of the Fund. Moreover, judgements about effectiveness and impact have to be reached in the context of the opaqueness and often protracted nature of the PRC's internal processes. The high priority the authorities attach to training, which has inherently long-term payoffs, compounds this challenge.

34. As of end-2020, only 17 projects were included in the RBM database; of these, most had objectives and outcomes defined, but only around two-thirds of the defined outcomes were rated (see Figure AI.1, Annex I). PRC officials interviewed did not demonstrate a high level of familiarity with the Fund's use of an RBM approach, while some staff sensed a creeping concern among officials that RBM log frames and ratings might be misconstrued as a framework for judging the performance of the authorities.

35. Moreover, significant elements of the Fund's CD to PRC do not readily lend themselves to being easily captured by the RBM system. For example, in the area of statistics, the authorities have not sought programmatic CD support; rather STA's engagement has been largely piecemeal and focused on training and on advice to facilitate subscription to the SDDS. Equally, the effectiveness and impact of inhouse CD provided by MCM's Senior Financial Sector TA Advisor has largely depended on the benefits of continuous engagement behind closed doors. More generally, the process of relationship building has the potential for significant longer term systemic payoffs which cannot currently be easily assessed.

36. Nonetheless, on some workstreams, there is tangible evidence of uptake of recommendations and broader impact. In particular, an examination of the three successive 3-year workplans agreed with SAT, including agreed log frames and mid-term evaluations for the

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<sup>12</sup> There have been rare occasions when CD reports have been published at the request of the authorities, for example the 2018 report on "Tax Policy and Employment Creation," IMF (2018d). See Table AI.2 in Annex I.

first two workplans<sup>13</sup> demonstrates a significant contribution to the PRC's tax policy and administration reform agenda. On policy, this has included the reform of PRC's value-added tax (VAT) (replacing earlier service business taxes) and improvements in the treatment of exporters, consolidation of personal income tax rates, centralization of social security arrangements and their more effective integration within the tax system and strengthening capacity to analyze the economic impact of tax reforms. On administration, FAD CD has supported the implementation of the authorities' agenda<sup>14</sup> with advice on legal frameworks, compliance strategies, personal income tax administration, strengthened taxpayer services, auditing and investigations, and performance measurement. The first two workplans were assessed as fully meeting expectations. Arguably more tellingly, the SAT has repeatedly demonstrated the value it sees in IMF CD by readily agreeing to jointly Fund successive workplans—and most recently, inviting the Fund to comment on its internal March 2021 Strategy for Reform of Tax Collection and Administration. SAT officials spoke of the Fund's contribution in helping to localize recommendations for implementation. They emphasized the significance of Fund advice on public consultation and reforms such as the shift to targeted post-filing auditing, facilitating the integration of important social policy objectives through streamlined deduction arrangements, highlighting the latter as an example of broader impact.

37. The authorities have clearly been open to engaging on a range of follow-up CD to the 2011 and 2017 FSAPs.<sup>15</sup> The appointment of the Senior Advisor to the PBoC is itself testimony to progress in building relationships and trust, and there is circumstantial evidence he was influential on several aspects of efforts to operationalize macro-prudential policy, for example, the subsequent adoption of counter-cyclical capital buffers and the need for clear criteria to both trigger and turn-off macro-prudential measures. And there is anecdotal evidence of influence on related fronts, such as assisting the PBoC's approach to its public communication role, notwithstanding sensitivities about engaging on the mechanics of monetary policy more generally. On the other hand, the authorities have expressed little interest in IMF CD on monetary policy or capital account issues, notwithstanding the attention on these issues in surveillance engagement.

38. The track record of engagement with CSRC and, even more so, CBIRC, remains too short to form definitive judgements. CSRC recent officials are nevertheless complimentary regarding activities delivered under its MoU with the Fund, consistent with feedback reported in relevant back-to-office reports. CBIRC officials were positive about the value of earlier training courses provided through the China Training Program and Singapore Institute and expressed optimism about the CD relationship still to be operationalized under the 2019 MoU.

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<sup>13</sup> The authorities did not agree to include a logframe in the 2019–2021 Workplan while the planned midterm evaluation has been delayed because of COVID-19.

<sup>14</sup> The SAT's "Blueprint for Deepening the Reform of Collection and Administrative Systems of State and Local Government Tax Administration."

<sup>15</sup> FSAPs are classed as surveillance and therefore fall outside the scope of this study.

39. CD engagement with the MoF has a longer history but is also difficult to assess.<sup>16</sup> The establishment of a well-designed TSA is seen as a success by staff. CD on financial reporting and balance sheet issues (including accrual accounting) probably contributed to policy actions by the authorities to improve provincial level budget reporting and address debt issues, but its direct impact is difficult to isolate and verify.<sup>17</sup> The authorities' response to the CD on medium term budgeting issues between 2014–2016 remains opaque, while recent efforts commencing in 2019 to re-engage on macro-fiscal issues have reportedly elicited interest in other country experience but a reluctance to discuss domestic policy options.<sup>18, 19</sup>

40. Officials have uniformly provided positive feedback on the value of the CICDC's activities in its first few years. In the absence of an agreed formal evaluation process comparable to that followed by the RCDCs, the primary test of effectiveness will be the willingness of the authorities to consider renewal of the funding arrangement in due course.<sup>20</sup>

41. However, the CICDC's role in the Fund's ability to respond quickly to the authorities' interest in debt sustainability analysis is worth highlighting. Officials have been very positive about the course. Perhaps more importantly, they have indicated that this engagement also fed into work on the debt sustainability framework subsequently announced at the second Belt and Road Forum in April 2019. Despite debate in some quarters regarding the merits of the PRC framework, the Fund has been able to constructively engage the authorities on an important issue which has proven difficult for other external partners,<sup>21</sup> underscoring the importance of continuing efforts to build on the relationship.

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<sup>16</sup> As of the time of drafting, the author has not been able to obtain direct feedback from MoF officials.

<sup>17</sup> The World Bank was also active on the issue of Local Government debt, but also notes the difficulty of assessing the extent of any contribution to the 2016 decision on budget support.

<sup>18</sup> Staff do not have a good feel for the current standing and capacity of the Macro-Fiscal Unit within the MoF. The pandemic required the second of two workshops on this issue, in 2020, to be run virtually which also limited the scope for engagement. Nonetheless, FAD is currently considering a list of requested follow-up activities from the MoF and a further virtual workshop is expected this year.

<sup>19</sup> Challenges in reaching agreement with the MoF on the specifics of the "joint funding" principle under the MoU may also be stymieing engagement under the MoU, although is relatively easy to navigate in a world of "virtual delivery" and hence low costs.

<sup>20</sup> Participant feedback on individual courses is not collated by the CICDC but collected by the department responsible for the design and delivery of the course, and the mechanisms for doing so vary by department. While one might expect the feedback to be broadly in line with that of participants in all Fund courses, it is difficult to easily test whether the tailoring of CICDC courses results in systemically higher participant ratings.

<sup>21</sup> For example, concerns about debt sustainability issues associated with BRI led, inter alia, to a PRC proposal, developed by the MoF, for a Multilateral Center for Cooperation of Development Finance (MCDF) which would raise standards for cross border infrastructure financing. The World Bank's decision not to host the MCDF led eventually to it being established with secretariat support from the Asian Infrastructure Investment Bank. Notwithstanding a robust governance design, the standing and effectiveness of the MCDF has arguably been compromised by the reluctance of major donors to support it in the current difficult geopolitical environment.

### III. OVERALL ASSESSMENT

42. The relevance of Fund CD to PRC has been anchored by the policy dialogue and driven by country demand. Within this overall approach, a combination of long-term relationship building and a degree of flexible entrepreneurship on the part of the Fund has served to ensure a mix of CD activities which, while piecemeal, has nonetheless coherently focused on the overarching task of modernizing policy and regulatory frameworks for a more market driven economy with net positive spillovers for others. Effectiveness and impact need to be judged broadly against the Fund's multi-layered objectives.

#### Relevance

43. The Fund has positioned itself to respond to CD requests which align with key areas of focus for surveillance. The longstanding relationship with the SAT has facilitated a significant engagement on modernizing systems and improving the interface between tax and welfare arrangements. The establishment of relations with financial regulators allows for follow up on core FSAP recommendations. The location of a Senior Advisor in the PBoC facilitated focused hands-on advice on the development of macro-prudential policy frameworks and tools. Efforts to deepen the engagement with the MoF have offered the opportunity to complement earlier work on downstream issues (such as the TSA) with more of an upstream—and holistic—focus on balance sheet issues and macro-fiscal frameworks. The focus on improving domestic policy and regulatory frameworks also indirectly addresses the strategic goal of helping shape PRC's regional and global impact, while the nimble response to the authorities' interest in debt sustainability issues, as an increasingly significant international creditor, is clearly directly relevant to this.

#### Coherence

44. The Fund's country strategy provides a clear high-level framework—focused on supporting adaptation to markets and acknowledging PRC's increasing systemic importance in terms of both global/regional spillovers and its potential as a partner on global public goods—to guide coherence. However, the strongly demand-driven determination of specific activities combined with PRC's siloed institutional culture has meant that the pattern of CD has not been as holistically integrated as one might wish.

45. For example, the authorities' take up of CD in the fiscal policy area, outside of tax issues, has clearly been more piecemeal than the Fund would have preferred. There has been limited interest in addressing weaknesses at the national level in government financial reporting notwithstanding sustained efforts in the context of surveillance to raise awareness of the implications for effective macroeconomic policy. Engagement on statistics issues more generally has been patchy. Similarly, while open to CD on financial sector and macro-prudential issues, the PBoC has been more reluctant on monetary policy mechanics or capital account liberalization. And the limited relationship with the NDRC has necessarily narrowed the scope for CD on macroeconomic policy frameworks.

46. In practice, the efforts of suitably opportunistic and entrepreneurial resident representatives, drawing on local knowledge and relationships, has helped nudge demand on key issues—such as debt sustainability and, potentially, emerging interest in macro-fiscal frameworks. This is likely to remain crucial to addressing gaps and enhancing coherence over time.

### **Effectiveness, Impact, Sustainability**

47. The evidence suggests that the Fund has made important progress in broadening and, in some cases deepening, important CD relationships within PRC, as reflected in the establishment of the MoU/LoU architecture and the CICDC, as well as through investment in the continuity of personal relationships. This will remain central to achieving the Fund’s multi-layered objectives set out in its country strategy. Nonetheless, an assessment of the overall effectiveness and impact of the Fund’s CD activities to date requires realistic benchmarks in the context of what invariably needs to be seen as long game playing out in an idiosyncratic operating environment.

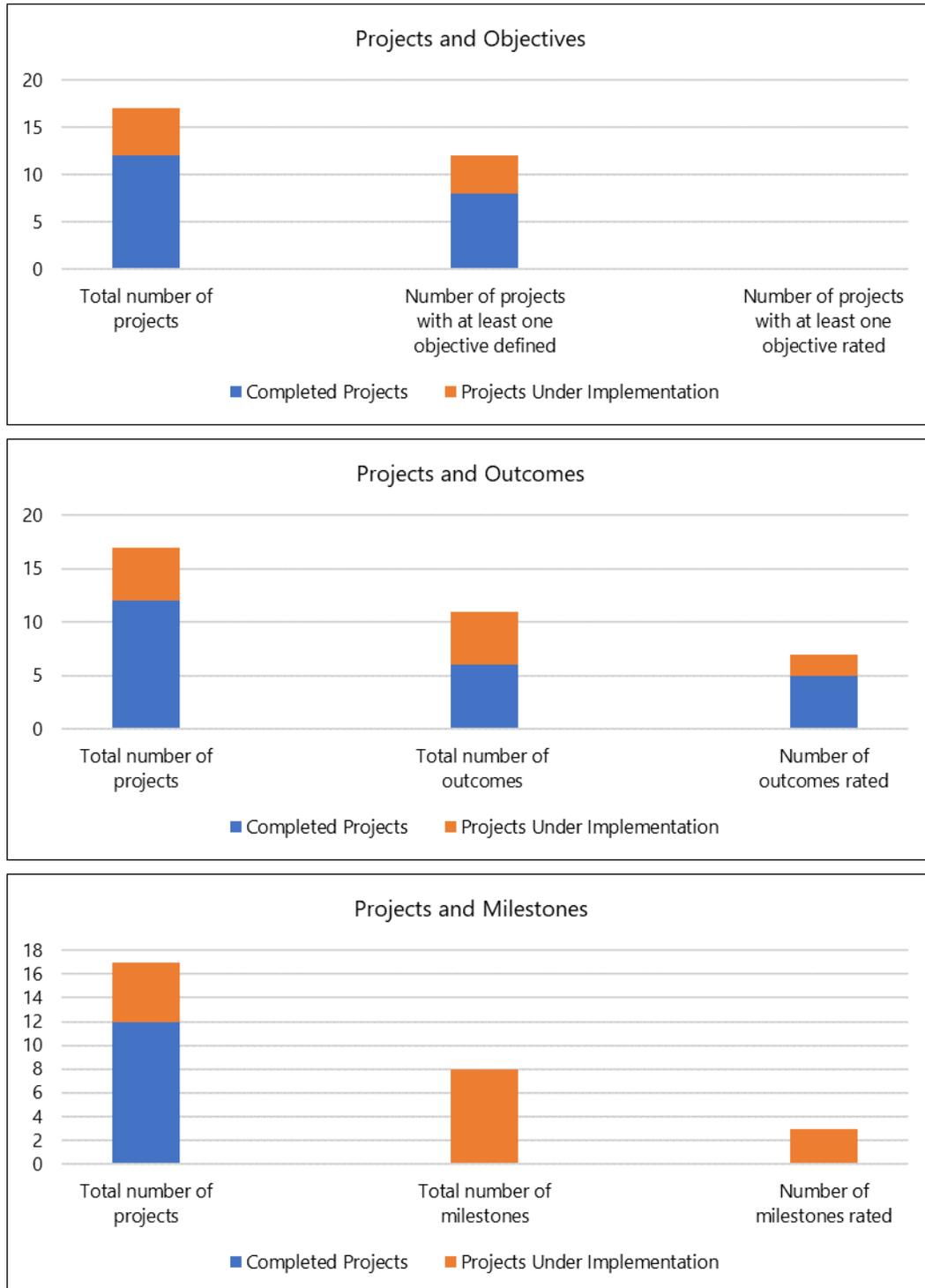
48. Staff have emphasized the need to invest significant effort over the last decade to raise awareness across the Chinese system of what the Fund can offer in terms of CD, how it might differ from say, outsourced World Bank TA, etc. There are clearly workstreams, such as with the SAT, where protracted engagement has been highly effective with significant impact and sustainability underpinned by strong ownership, which offer a potential model for others, if practical issues regarding “joint funding” can be managed. Other success stories include the contribution of the Senior Adviser on macroprudential and associated policy frameworks and tools (itself testimony to the benefits of relationship building) and the work on debt sustainability analysis. The story regarding engagement with the MoF appears more mixed although not without early success (e.g., TSA) or promise in areas such as macro-fiscal policy, while other counterpart relationships (CSRC, CBIRC) will need time—and importantly, continued investment of effort—to produce tangible results.

49. The CICDC has been widely welcomed by counterparts and, while not subject to the evaluation requirements that apply to RCDCs, will face the ultimate market test when the current funding arrangements are revisited. The significance of its ability to engage on sensitive issues such as debt sustainability in the context of the BRI should not be understated.

50. As the experience with the SAT demonstrates, a demand-driven model and effective domestic institutions will underpin the sustainability of agreed individual workstreams. However, the overall sustainability of the Fund’s strategic approach is inevitably hostage to exogenous factors, such as the authorities’ continued commitment to expanding the domestic role of markets and the potential need to navigate an increasingly difficult geo-political environment. More immediately, efforts appear to be needed to reinvigorate contact with some counterparts disrupted by the pandemic, while continuing to invest in the relationship building throughout the Chinese system, especially at the senior level, which has provided the foundation for the Fund’s growing CD relationship to date.

## ANNEX I. CD ACTIVITIES FOR PEOPLE'S REPUBLIC OF CHINA

**Figure AI.1. PRC—Results Based Management Data on Projects, Objectives, Outcomes, and Milestones**



Sources: IMF, RBM data; IEO staff calculations.

**Table AI.1. PRC—Number of Missions, 2012–2020**

Year	FAD	ICD	LEG	MCM	RES	STA	Others	Total
2012	6	0	0	0	0	4	2	12
2013	8	3	1	1	0	2	0	15
2014	15	6	2	4	0	4	1	32
2015	20	5	0	2	0	2	0	29
2016	16	4	4	8	0	5	0	37
2017	12	7	1	1	0	1	1	23
2018	12	11	3	3	0	1	1	31
2019	13	5	1	6	0	1	1	27
2020	10	4	2	9	2	2	1	30
Total	112	45	14	34	2	22	7	236

Sources: IMF, TIMS data; IEO staff calculations.

**Table AI.2. PRC—List of TA Reports, 2012–2020**

	FAD	MCM	STA	LEG	STA/MCM	Total	Of which		
							Available within IMF	Available but confidential	Published
2012	0	0	1	0	0	1	0	0	0
2013	2	0	0	0	0	2	1	1	0
2014	4	0	0	0	1	5	2	2	0
2015	5	0	1	0	0	6	4	1	0
2016	3	0	0	0	0	3	1	2	0
2017	0	0	0	0	0	0	0	0	0
2018	2	0	0	0	0	2	1	1	1
2019	4	0	0	0	0	4	1	0	0
2020	1	0	0	0	0	1	0	1	0
Total	21	0	2	0	1	24	10	8	1

Source: IMF, Institutional Repository.



# **INDONESIA**

**DAN CITRIN\***

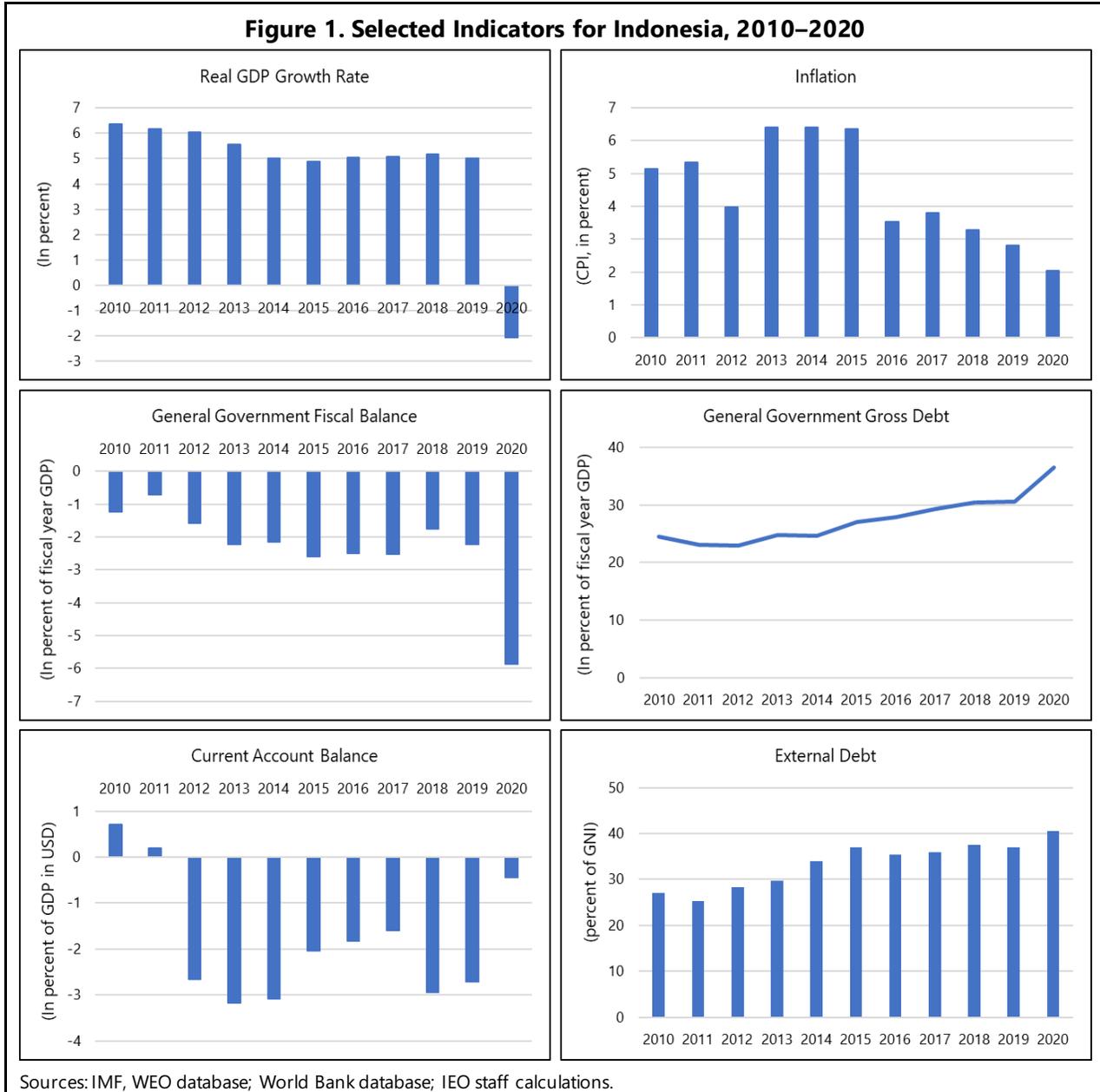
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\* Consultant, Independent Evaluation Office of the IMF.

## I. INTRODUCTION AND COUNTRY OVERVIEW

1. In the ten years prior to the onset of the COVID-19 pandemic, Indonesia enjoyed stable economic growth in the context of prudent macroeconomic management. Real GDP growth averaged 5 percent per year, annual inflation hovered around 3 percent, the budget deficit and government debt were low, and the banking sector was well capitalized (Figure 1). The admirable performance was supported by a favorable policy framework that included an inflation targeting regime, fiscal rules, and banking regulations broadly in line with international standards.

**Figure 1. Selected Indicators for Indonesia, 2010–2020**



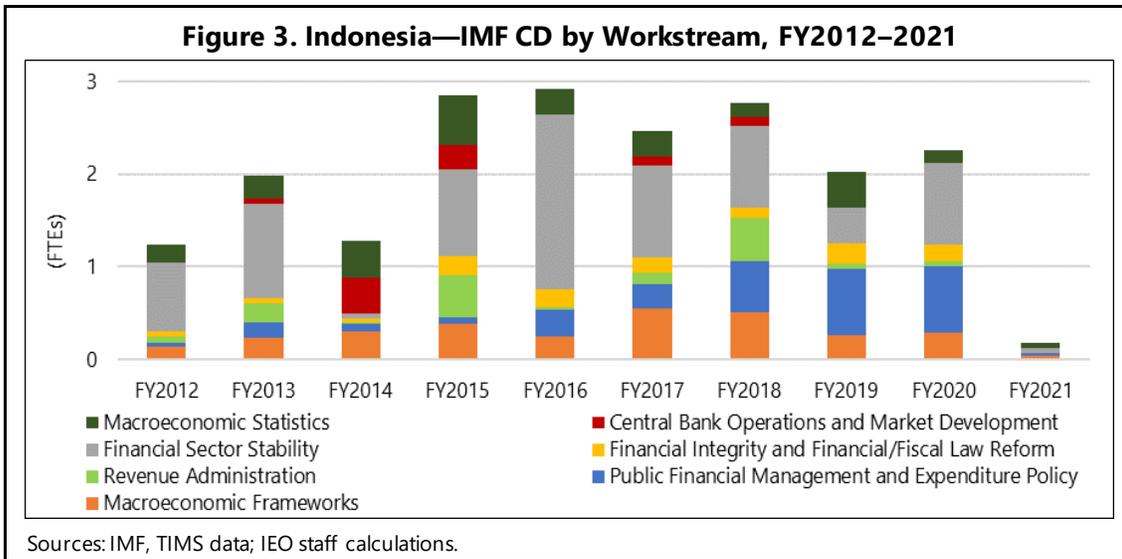
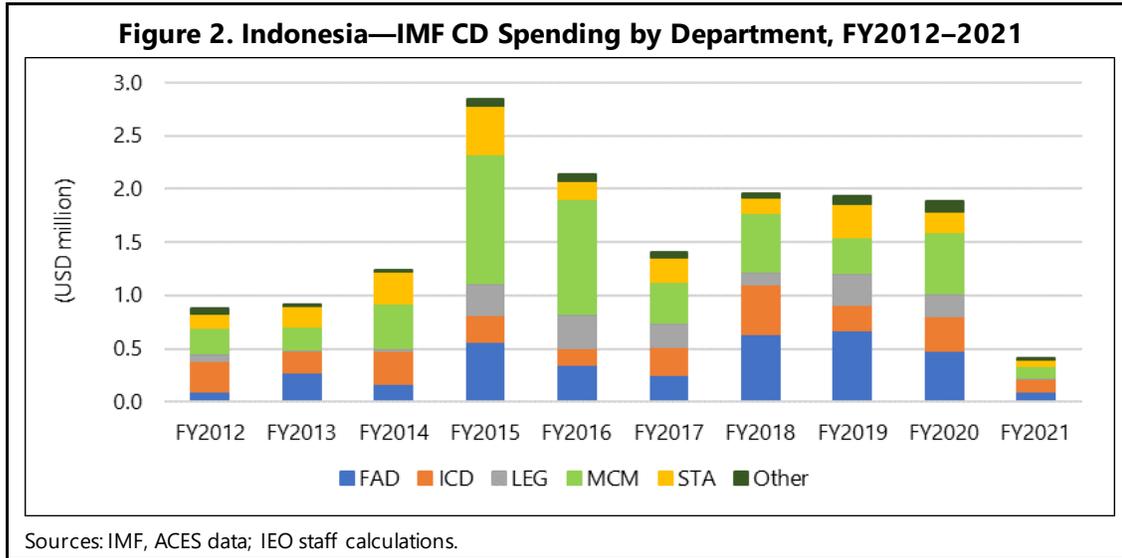
2. Like other countries, Indonesia was hit hard by the impact of COVID-19. Real GDP fell by 3½ percent in the first half of 2020 (seasonally adjusted), owing to domestic containment measures, and international travel restrictions, and spillovers from the global slowdown. With the easing of some containment measures and the introduction of a bold and comprehensive policy package that included successive fiscal packages and a series of steps to ease monetary policy and provide liquidity support to banks, the economy rebounded in the second half of year. Nevertheless, real GDP fell by almost 2 percent in 2020 as a whole and is projected to grow by about 4¼ percent in 2021 (October WEO), below its pre-COVID trend.

3. Indonesia's growth performance prior to COVID allowed it to reach *upper* middle-income status in 2020 and become the world's tenth largest economy in purchasing power parity terms. At the same time, over the past decade Indonesia cut its poverty rate by more than one-half, to just under 10 percent in 2020. Nevertheless, many challenges confront Indonesia's medium-term outlook. Large uncertainties to the growth outlook related to vaccine distribution and the persistence of the pandemic in Indonesia increase the risk that a large vulnerable share of the population could fall back into poverty. At the same time, labor productivity remains low, with the World Bank's Human Capital Index showing Indonesia as lagging both its regional peers and others of upper middle-income status. To address human capital needs will require increases in health and education spending, which consistently lag Indonesia's comparators. But this task will be difficult: Indonesia's revenue ratio is relatively low while maintenance of fiscal credibility will require the gradual unwinding of the exceptional fiscal support in 2020. Furthermore, a host of structural reforms to improve Indonesia's infrastructure and enhance the weak business climate by easing regulatory restrictions and strengthen governance remain important for improving competitiveness.

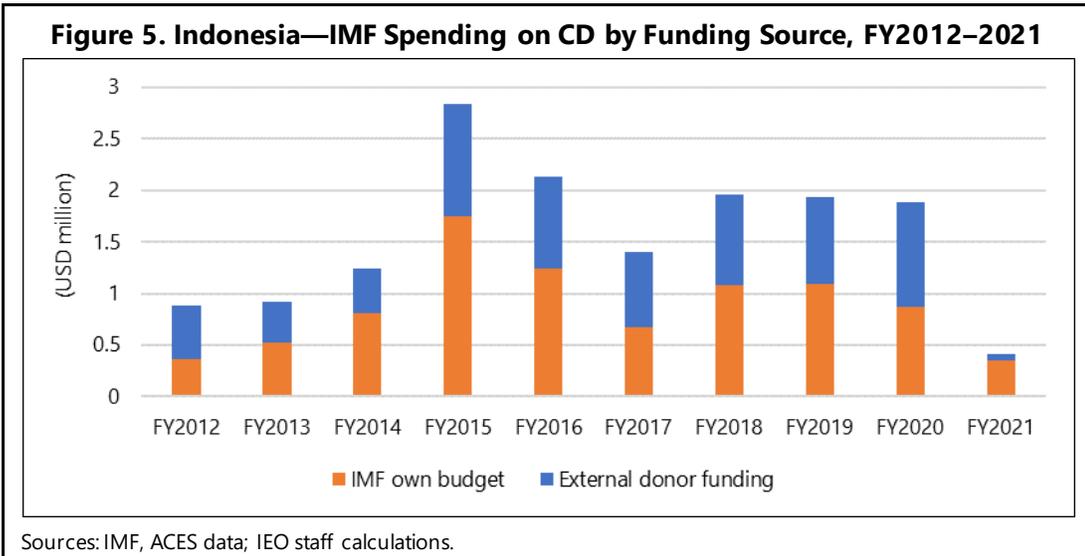
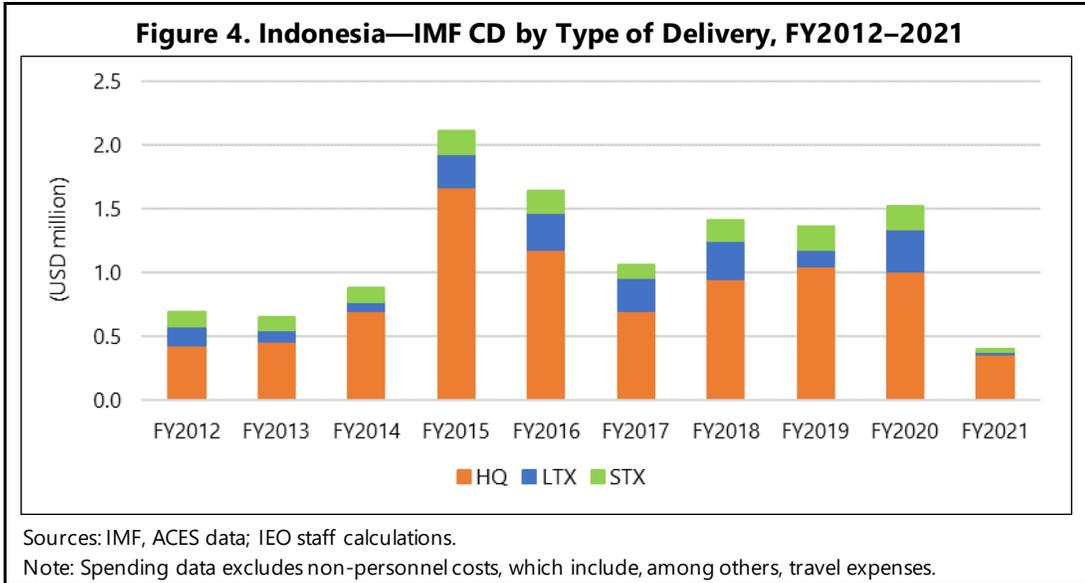
4. Indonesia represented the eleventh largest user of IMF CD in Asia during 2012–2020 (see Table 1 in Overview). Although less extensively than to the other two countries examined in this study, the IMF provided CD to Indonesia in the context of a surveillance engagement on an ongoing basis. Fund staff have been keen to continue to build its new engagement with Indonesia following a relationship previously dominated by several Fund-supported programs and post-Asia crisis management, and have been very responsive to requests for TA and training from the authorities. Over the period as a whole, MCM has been the largest provider of CD to Indonesia. During the most recent three years, FAD and MCM have provided broadly equal amounts (Figure 2).

5. Most of the assistance provided by MCM during this period was in the area of strengthening macro-prudential regulations and bank supervision (Figure 3). With the exception of 2014 and 2018, a Fund expert resident in Jakarta provided TA to the Indonesian financial supervisory agency (Annex I, Table AI.2). In addition, assistance related to crisis prevention and deepening financial markets was provided in 2016. FAD provided assistance related to both strengthening revenues and improving public financial management: (i) TA in 2017 on tax policy and tax administration reforms; (ii) Indonesia's Public Investment Management Assessment in

2019 which listed priorities to improve public investment management; and (iii) a public sector balance sheet analysis in 2019 aimed at improving fiscal reporting. With the exception of the long-term advisor for banking, most of the CD was provided by HQ staff that recommended reforms in the context of traditional missions from Washington (virtual during COVID-19) (Figure 4). Indonesia does not participate in an RCDC, although it does benefit from training support from STI.



6. Roughly one-half of IMF TA to Indonesia during 2012–2020 was financed by external donors (Figure 5). Almost all of this external financing was provided by Japan. The Anti-Money Laundering/Countering the Financing of Terrorism (AML/CFT) trust fund financed advice in the area of anti-money laundering by LEG during the latter six years of the period.



**II. CD ENGAGEMENT**

**A. Strategy, Prioritization, and Allocation**

7. Notwithstanding the restoration of macro-financial stability during the previous decade and the maintenance of sound macro policies during 2012–2020 in Indonesia, there was broad demand for policy reforms to enhance medium term growth and deal with the development challenges noted earlier. The authorities also were interested in assistance of a more technical nature to improve the functioning of financial markets and respond to developments in international markets.

8. The mix of IMF CD that was provided to Indonesia primarily reflected responses to specific requests by the authorities. As such, the assistance did not necessarily represent priority allocations determined on the basis of a comprehensive strategy developed by the staff together with the authorities.<sup>1</sup> This situation reflected several inter-related factors. Given Indonesia's status as a large emerging market economy and its relationship with the IMF (and the international community) in the past, high political sensitivities remained regarding the formulation of any policy strategies involving the Fund and other external actors. Thus, even in the area of TA or training, all stakeholders took care to avoid the possibility of stigma associated with a strategic framework developed with the heavy explicit involvement of external institutions.

9. Nevertheless, the authorities remained interested in taking advantage of the IMF's international expertise and made requests for assistance in a number of specific areas. And, as noted by both the authorities and IMF staff, with the Fund paying special attention to strengthening its engagement in Asia and with Indonesia in particular, the institution was highly responsive to these requests. And in this context, coherent reform strategies were formulated on specific policy issues, such as financial sector supervision and regulation, treasury management, and fuel subsidy reform.

10. While the authorities largely were in control of the CD agenda, there was substantial dialogue between IMF staff and the authorities to shape the nature and scope of the assistance provided. The authorities met with CDDs at the Annual and Spring meetings, and discussions were held during the Article IV missions and other staff visits to Indonesia. This dialogue was facilitated by the ongoing participation of FAD and MCM staff on surveillance country teams. A key role in the dialogue between the authorities and staff was played by successive IMF resident representatives in Jakarta, who provided input on policy areas where assistance might be requested and also helped resolve any questions or issues that might arise in planning the CD provision.

11. As would be expected given the primacy of the authorities' role in the planning process, ownership of the IMF CD was overall strong, particularly among senior officials. However, interviews did indicate cases where ownership was inconsistent, and hampered effective implementation. Notable examples related to the effectiveness of the role played by the Fund's long-term advisors assigned to the financial supervision agency, and to the buy-in of senior tax officials to the work done by FAD on tax policy and administration reforms (see paragraph 18, and discussion in paragraphs 25–27).

12. Cases of weak ownership and ineffective implementation did appear to lead to caution in CDDs to provide additional assistance in associated areas. However, any impact of results on

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<sup>1</sup> A CSN for Indonesia has not been prepared since 2015, when the preparation of country CD strategy notes for all countries as a general practice was terminated in APD. Since then, the Indonesia team's TA priorities were summarized in a TA-surveillance country matrix prepared as input for the annual exercise coordinated by ICD the plan CD activities.

allocation and prioritization appears to have been ultimately superseded by the desire to be responsive to the authorities' requests and thereby strengthen engagement.

13. Given the nature of the strategic planning process for CD in Indonesia, its integration with surveillance was of course less advanced than cases of an intensive collaborative planning process involving the authorities and staff (e.g., as for Cambodia). While there has been increasing integration in most recent years, the coverage of CD in recent Article IV documentation, for example, is less extensive than in other APD cases. With political sensitivity to any hint of stigma still high, it would seem that further steps towards integration would need to be low key in approach, though the IMF should still have an explicit strategy. The authorities indicated strong interest in learning from the IMF in new topics such as fintech, digital currencies and international taxation. They suggested that the IMF should position itself to provide advising in the context of Article IV surveillance and follow-up TA.

## **B. Delivery**

14. Discussions with relevant stakeholders suggest that the advice provided to Indonesia in the context of IMF CD was generally of high quality and well-tailored to country circumstances. Given the institutional importance of a strong and healthy engagement with the country, and with TA requests often conveyed by the authorities to the Fund at the highest levels, CDDs paid special attention to Indonesia. Interviewees noted that work in Indonesia always seemed to attract the best staff and external experts, often with previous experience or good knowledge of Indonesia's particular circumstances.

15. As illustrated in Figure 4, TA to Indonesia was mainly delivered by visits (missions) of HQ staff supplemented by STXs, as well as successive resident long-term advisors for banking supervision issues. Compared with other cases, there was no role for experts located in a RCDC. Reliance on expertise from HQ was in line with the preferences of the authorities, who stressed that they looked to the Fund to learn from best international practice and insights on latest issues and challenges facing the global community. That said, in areas where the capacity of the authorities was relatively weak, the use of resident experts was desirable. The authorities placed less priority on participation in an RCDC or peer-to-peer learning opportunities provided by the Fund, noting that: (i) they valued most the Fund's pool of HQ-based international expertise centered; and (ii) they already participated in considerable peer-to-peer seminars and other such events in the context of various Asian groups, including Association of Southeast Asian Nations (ASEAN).

16. There remained heavy demand for training, notably at the STI, reflecting its convenient proximate location. Indonesia also made frequent use of seminars and workshop training opportunities, both on-site and virtual (most recently). The authorities had a positive assessment of the training provided by the IMF, and suggested efforts continue to be made to escalate capacity in this area.

17. The use of virtual modes of engagement since the onset of the COVID-19 pandemic has appeared to work relatively well in Indonesia's case. Notwithstanding difficulties posed by time zone differences, good internet connectivity facilitated communication between staff and the authorities. That said, the authorities noted that face-to-face contacts remained important both to build relations and also facilitate certain practical knowledge dissemination. For example, it was noted by Bank Indonesia (BI) officials that workshops involving sophisticated model simulations needed to be held in Jakarta to be effective.

18. Notwithstanding the overall high quality of expertise and favorable assessment of the modes of deliver, several issues emerged in the course of the review:

- A number of interviews noted that IMF CD recommendations were designed well and generally framed with appropriate regard for Indonesia's circumstances, but greater attention needed to be paid to follow-up and assistance on implementation. This feedback was notable for the early part of the review period. In such situations, the resident representative's own initiative and efforts were essential to facilitate follow-up to TA recommendations. These observations point to the need for a continuous dialogue with the country team at the center of the engagement. The integration of CD and surveillance, with the explicitly mandated involvement of the area department mission chief, was seen to be essential to ensure a more systematic approach in this regard.
- The authorities noted that in a couple of cases, most recently in the case of MCM TA that was provided on central bank communications, recommendations were not appropriately tailored to country circumstances and therefore not able to be implemented. The authorities noted that their views and comments were not adequately taken into account by the IMF's team of experts.
- Given the investment, due care is needed when the IMF agrees to provide a long-term resident advisor. In one case, when the IMF sent a LTX to advise Indonesia's financial supervisory agency, the expert—reportedly sent without a clear TOR and work agenda—was not initially welcomed by staff and had a hard time getting access to officials. Stronger accountability with greater attention to results would seem to have been warranted in this case.

### **C. Partnerships and Coordination**

19. Coordination with other CD providers was led by the IMF resident representative, who sought to communicate informally with the World Bank and ADB country located in the field. There were no formal arrangements for coordination or partnerships amongst the CD partners and donors. Due to political sensitivities, the authorities opposed any formal mechanisms or regular meetings involving multiple stakeholders. Interviews suggest that the success or depth of communications efforts depended on the personalities involved, with the dialogue not always a

close one. Coordination was also driven by specific CD programs—for example, FAD coordinated quite well with Bank colleagues to minimize duplication in their CD efforts.

20. On monetary policy and financial sector matters, the IMF was clearly acknowledged as the institution of choice for TA and training. On other issues, however, the division of labor was often less clear, and with the World Bank having a large field presence in Jakarta, lack of ongoing communication implied the risk of competition and overlap. In fact, it was suggested by some that the Bank was often relied on to provide advice in areas (e.g., fiscal policy) that would be considered to be in the IMF's purview. At least one senior official indicated that they occasionally did take advantage of Bank-Fund competition to gain different perspectives on policy challenges. Notwithstanding the risks, the authorities were not aware of substantial overlapping or duplication in CD delivery amongst providers.

21. One interviewee suggested that the lack of close coordination and partnerships combined with political sensitivities surrounding working with foreign institutions (particularly the IMF), complicated follow-up and effective implementation. An alternative model could be one where: (i) the IMF CD experts took the lead in determining how best to employ international experience and best practice; (ii) the country team (resident representative and mission chief) monitor follow-up and facilitate active engagement by relevant stakeholders; and (iii) the IMF rely on partnerships with local partners to assist the authorities with implementation.

22. Finally, in this area, the authorities support publication of TA reports and recognize the benefits of learning from the experience of peers on dealing with similar policy challenges. That said, while most reports are available within the IMF, with very few exceptions they have not been published externally (See Annex I, Table AI.3).

#### **D. Impact and Effectiveness**

23. Discussions held with a range of stakeholders suggest that IMF CD to Indonesia has been effective when tailored and when ownership has been strong. CD provision to the central bank (BI) and the financial supervision agency (OJK) has been noteworthy in that regard. The Indonesian authorities pursued an ambitious agenda to promote financial deepening along with strengthening macro prudential supervision and crisis management over the last decade. Notwithstanding progress, the 2017 FSAP Update identified significant weaknesses that still hindered stability and inclusive growth. The IMF then provided CD to help address certain priority challenges: (i) IMF TA supported the improvement of BI's stress-testing capabilities and framework; (ii) the OJK issued new regulations enhancing supervision of financial conglomerates that took account of IMF TA recommendations; (iii) IMF TA helped the OJK implement stronger credit and risk management regulations in line with IFRS9; and (iv) the IMF Legal Department helped strengthen the OJK's supervision and regulation of AMF/CFT risks. Also, IMF TA supported the fiscal authorities to implement steps to increase the liquidity of its debt instruments.

24. CD has also helped BI reform and strengthen various operational tools to improve the effectiveness of monetary policy over a number of years, and also to develop a roadmap for financial deepening and inclusion. TA from the IMF has assisted to Indonesia strengthen its statistics to improve economic monitoring capabilities. In recent years, it has helped the authorities use big data to develop an enhanced residential property price index, expand the coverage of its producer price index to include service sector activities, and develop integrated sectoral accounts and balance sheet statistics. And finally, with respect to training, where there remains high demand, IMF staff note that the courses provided by STI are highly relevant and target the right officials, thereby creating a lasting impact.

25. At the same time, results of previous CD projects do not seem to be consistently taken into account to ensure adequate implementation and positive outcomes when undertaking new engagements. On occasion, demand for TA lies mainly with the leadership of a ministry or agency, such that ownership can easily dissipate with personnel changes or due to lack of wider political support, e.g., at the cabinet level. A high-profile example of CD provided in the face of unclear willingness for sustained implementation was the case of FAD's Medium-term Revenue Strategy project in 2017. Following a history of many years of TA provision with a patchy record of implementation, upon the strong request of the authorities, FAD provided CD and provided recommendations on a comprehensive medium-term tax strategy with reforms to both tax policy and administration. A unique feature of the strategy was that it featured an explicit link to the expenditure side, identifying sources of financing for key spending priorities over the medium term.

26. The IMF team engaged closely with the authorities on this project and its recommendations appeared to receive the initial endorsement of Ministry of Finance officials, but they ultimately were not fully owned and approved by Cabinet, and remain unimplemented. A detailed medium-term fiscal strategy backed by a broad set of measures adopted under a medium-term revenue reform framework was identified as a key priority by IMF staff in the 2020 Article IV Consultation. On their part, the authorities express their desire to explore all possible avenues to improve revenue mobilization despite political constraints. All this suggests that while the recommended reforms remain desirable, the implementation path may continue to be rocky.

27. Notwithstanding the lack of impact and perhaps some reputational damage to stakeholders involved, it is difficult to see what could have been done differently in this case. Given the request received from the highest levels to provide assistance on a critical policy priority, and the desire to provide support and enhance engagement with a key Fund member, the decision to provide assistance is difficult to question. At the same time, ownership could perhaps have been tested along the way, with endorsement sought for interim or partial reforms. Some have suggested also that the strategy recommended was too broad and ambitious, and that a more modest design may have had a better chance of successful implementation. More extensive communication and outreach efforts to build wider ownership may also have helped gain support, but the need for a low-key engagement in light of the need to avoid stigma may

have constrained such steps. RBM data is available for 22 projects; only 2 had their objectives rated though 26 of the total defined outcomes across the 22 projects were rated (see Annex I, Figure AI.1).

### III. OVERALL ASSESSMENT

28. Notwithstanding its strong macroeconomic track record over the last decade, Indonesia has continued to face significant medium-term development challenges and capacity-building needs. Accordingly, Indonesia has been a significant user of IMF TA and training over the past decade. While IMF CD can have an important role to play in the Fund's engagement with Indonesia in the period ahead, it should be recognized that past results have been mixed in some areas, and ensuring ownership will be critical to future success.

29. Looking back at IMF CD provision during 2012–2020, a number of positive attributes are evident.

30. The authorities were largely in control of the CD agenda, which fostered ownership. Where ownership was strong, IMF CD was effective and impactful, with actions taken in line with the recommendations of experts. The authorities looked to the IMF to provide international expertise, and the experts assigned to Indonesia were of high quality. With the strong engagement of the authorities and facilitated by intensive involvement of IMF resident representatives in Jakarta, TA recommendations were generally well designed with due regard to country circumstances. The authorities also benefitted significantly from IMF training opportunities, with the STI providing an ideal location with relevant courses that targeting the right officials.

31. At the same time, IMF CD to Indonesia could have been more effective in a number of respects. A stronger integration of CD with surveillance would have helped along in several dimensions. Formulation of a comprehensive CD strategy in the context of identifying key macroeconomic and development policy priorities, with the full involvement if not under the leadership of the authorities, is likely to have facilitated deeper ownership. Integration would also have helped ensure more consistent follow-up and attention to assistance with implementation of recommendations as needed. Recent indications of increasing integration are therefore welcome.

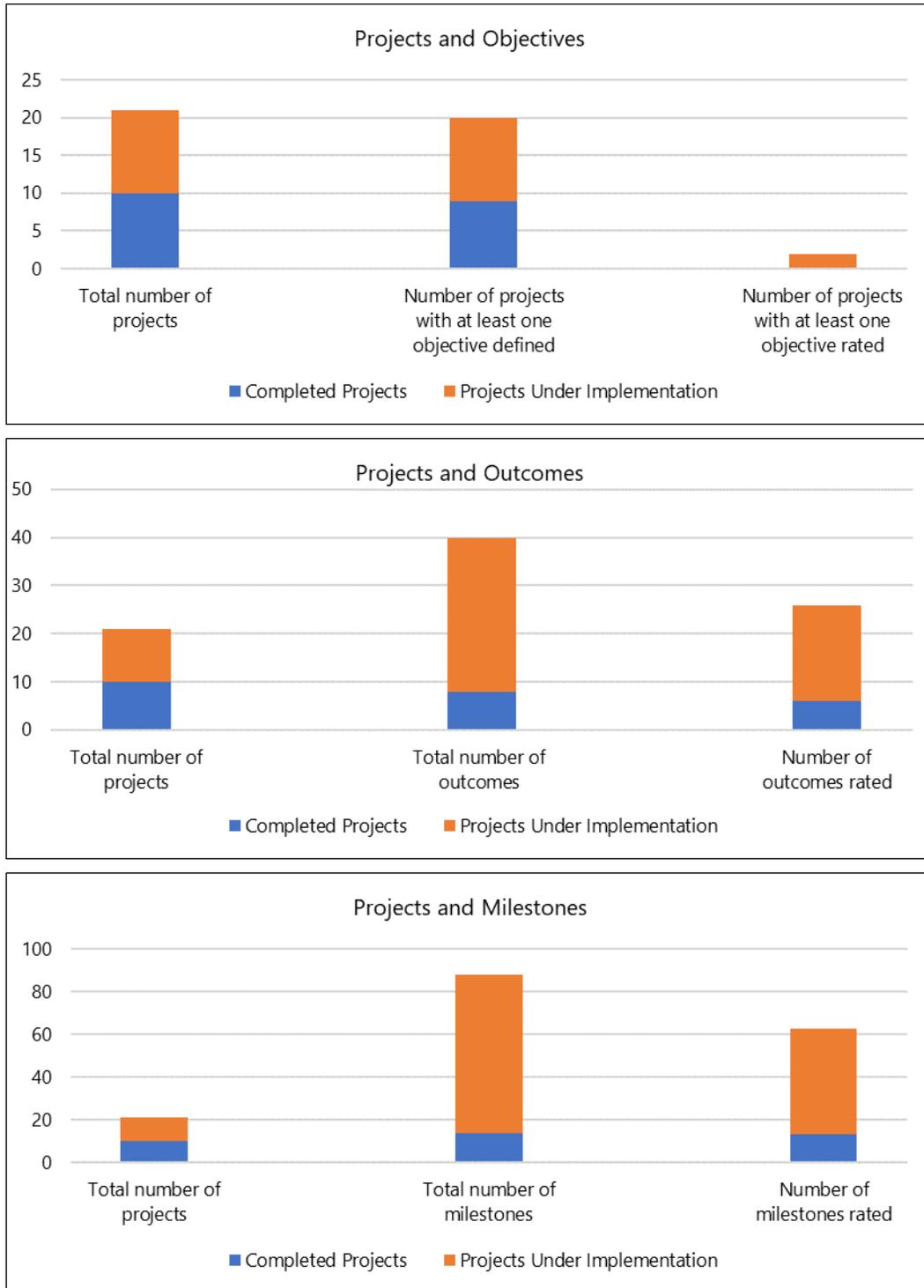
32. Perhaps more importantly, however, a more consistent use of expected outcomes, with milestones discussed and agreed ex ante with the authorities, and reference to previous results in planning future CD provision, would build ownership during the process. It would also help ensure that recommendations take appropriate account of country circumstances. Of course, use of results should be especially mindful of any remaining sensitivities of the Indonesian authorities in engaging with the Fund. Every effort should be made to put the authorities in the driver's seat and design a demand-driven set of agreed actions.

33. A few more lessons may be worth noting:

- In addition to ensuring high quality, attention to adequate on-boarding of external experts, as well as ensuring as much continuity of both staff and experts as possible, would be important to ensure CD provision is appropriately sensitive to country circumstances.
- Particularly in circumstances where ownership needs to be built over time, and capacity is weak, the gestation period of CD can be long. This points to the need for the Fund to stay engaged for an extended period. Milestones and expected results need to be calibrated with this in mind, and a more modest but more extended engagement focused on institution building and training may need to be the strategy in such instances.
- To the extent possible, the IMF may seek to work collaboratively with local partners in the implementation phase of CD projects. Such an approach would take advantage of knowledge of local conditions and also help avoid stigma.
- Finally, the IMF should take advantage of the strong demand for advice in new areas—policies to deal with climate change, green finance, digital currencies, modernization of central banking and monetary policy making, including the utilization of big data in policy making—and appropriately position itself in its areas of expertise. Such an approach could demonstrate the Fund’s usefulness as an expert partner while avoiding political sensitivities.

ANNEX I. CD ACTIVITIES FOR INDONESIA

**Figure AI.1. Indonesia—Results-Based Management Data on Projects, Objectives, Outcomes, and Milestones**



Sources: IMF, RBM data; IEO staff calculations.

**Table AI.1. Indonesia—Number of Missions, 2012–2020**

Year	FAD	ICD	LEG	MCM	RES	STA	Others	Total
2012	2	0	1	1	0	3	0	7
2013	5	0	0	2	0	4	0	11
2014	0	0	1	2	0	5	2	10
2015	2	0	4	7	0	4	2	19
2016	3	0	4	11	0	1	1	20
2017	7	0	4	1	0	4	7	23
2018	12	0	2	5	0	3	3	25
2019	9	0	3	3	0	6	2	23
2020	10	0	3	2	0	2	0	17
Total	50	0	22	34	0	32	17	155

Sources: IMF, TIMS data; IEO staff calculations.

**Table AI.2. Indonesia—Resident Advisors, 2012–2020**

Host institution	CDD	CD topic/workstream	Start date	End date
Central Bank	MCM	Bank Supervision & Regulation Advisor (Year 1)	10/2/2011	10/1/2012
Central Bank	MCM	Bank Supervision & Regulation Advisor (2nd Year Extension)	10/2/2012	5/18/2013
Central Bank	MCM	Resident Advisor to OJK on Conglomerate Supervision (Year 1)	1/30/2015	1/29/2016
Ministry of Finance	FAD	PFM Scoping on fiscal Decentralization	6/19/2015	6/29/2015
Central Bank	MCM	Resident Advisor to OJK on Conglomerate Supervision (2nd Year Extension)	1/30/2016	1/29/2017
Central Bank	MCM	Resident Advisor to OJK on Conglomerate Supervision (3rd Year Extension)	1/30/2017	1/29/2018
Central Bank	MCM	Bank Supervision & Regulation Advisor	4/10/2019	1/11/2020

Sources: IMF, Monetary and Capital Markets Department, Fiscal Affairs Department.

**Table AI.3. Indonesia—List of TA Reports, 2012–2020**

	FAD	MCM	STA	LEG	Total	Of which		
						Available within IMF	Available but confidential	Published
2012	0	0	1	0	1	0	0	0
2013	1	1	2	0	4	1	0	0
2014	0	4	2	0	6	2	0	0
2015	1	2	1	0	4	3	0	0
2016	0	4	1	0	5	4	0	0
2017	3	0	3	0	6	4	0	0
2018	0	1	4	0	5	1	0	1
2019	2	1	5	0	8	3	0	0
2020	1	0	2	0	3	2	0	0
Total	8	13	21	0	42	20	0	1

Source: IMF, Institutional Repository.

## **SRI LANKA**

**DAN CITRIN\***

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\* Consultant, Independent Evaluation Office of the IMF.

## I. INTRODUCTION AND COUNTRY OVERVIEW

1. Sri Lanka experienced a period of difficult macroeconomic performance during 2012–2020 (Figure 1). Real GDP growth averaged around 4 percent, but well below Sri Lanka’s medium-term potential—estimated at around 5½ percent.<sup>1</sup> Notwithstanding the expansion of tourism and IT sectors, growth was weighed down by political instability, a weak investment climate, and a narrow export base. More recently, the Easter Sunday terrorist attacks in April 2019 led to a sharp downturn in tourism and related activities. A subsequent gradual recovery was then disrupted by the onset of the COVID-19 pandemic, and output fell by 3½ percent in 2020. The outlook for 2021 and beyond is likely to be for only slow growth below potential. Aside from the risks associated with a further wave of COVID outbreaks, macroeconomic challenges stemming from high public debt, weak revenues, and low reserves, along with structural weaknesses reflecting a restrictive trade regime, weak investment climate, low female labor force participation, and a weak social safety net cloud the medium-term growth and development outlook.

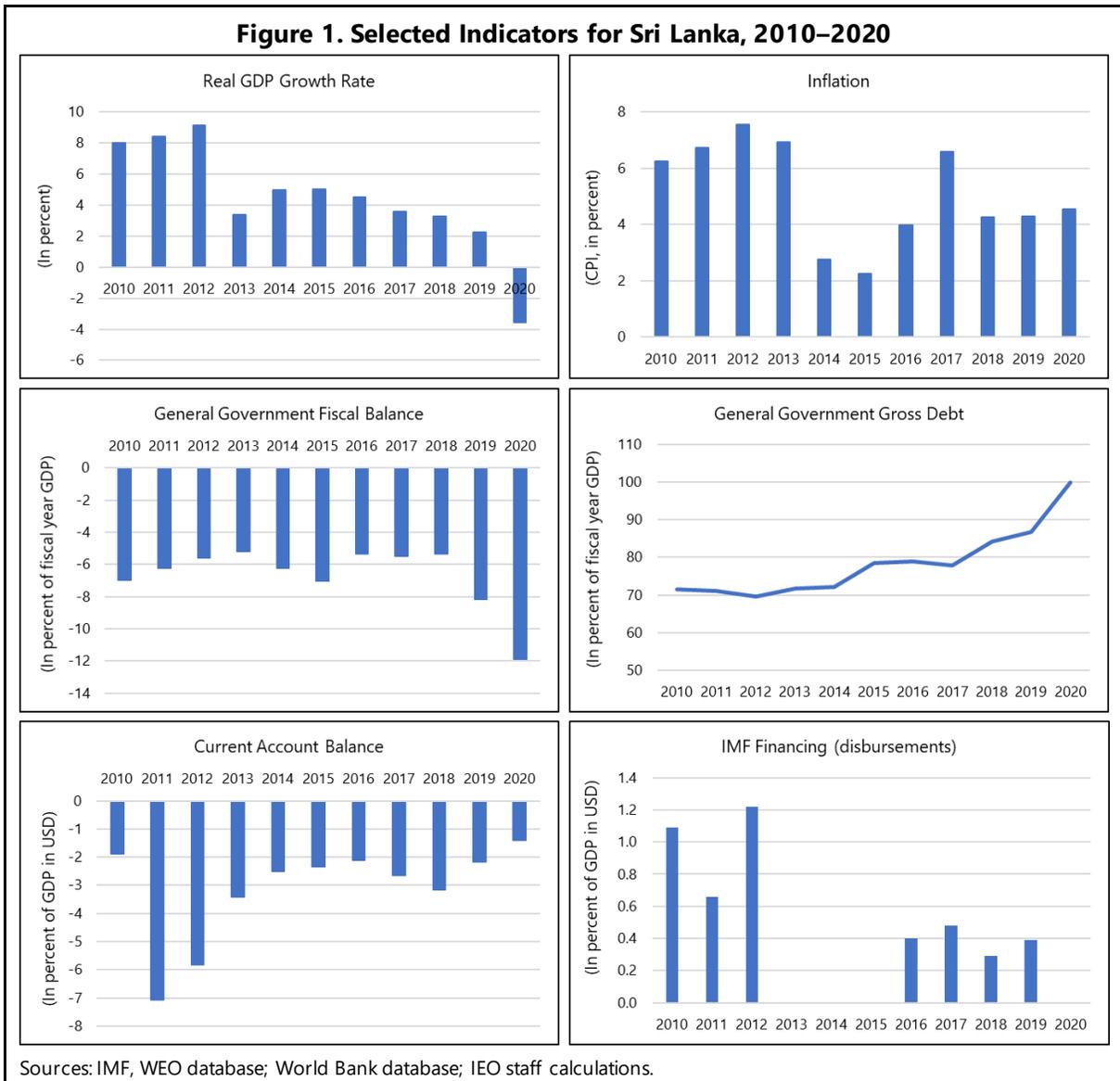
2. The COVID-19 pandemic has reversed previous progress in reducing poverty in Sri Lanka and jeopardized its aim of achieving middle-income status by 2025. After falling from 16.2 percent in 2012/13 to 9.2 percent in 2019, the World Bank estimates the poverty rate rose to 11.7 percent in 2020.<sup>2</sup> The increase in poverty reflected losses in jobs and earnings across a range of sectors, notwithstanding government measures to provide livelihood support. Sri Lanka ranks the highest in the World Bank’s Human Capital Index amongst its South Asian peers, but a host of policy actions would be desirable to unlock its growth potential and achieve its poverty reduction goals.

3. Sri Lanka was the seventh largest user of IMF CD amongst APD countries during the 2012–2020 review period (Table 1 in Summary). As indicated above, its economy experienced significant macroeconomic and financial instability over this period, and during much of the time the country had a program engagement with the Fund. Notably, the Extended Arrangement under the Extended Fund Facility covering the 2016–2019 period entailed wide-ranging actions to restore macroeconomic stability and advance structural reforms, and was heavily supported by Fund TA.

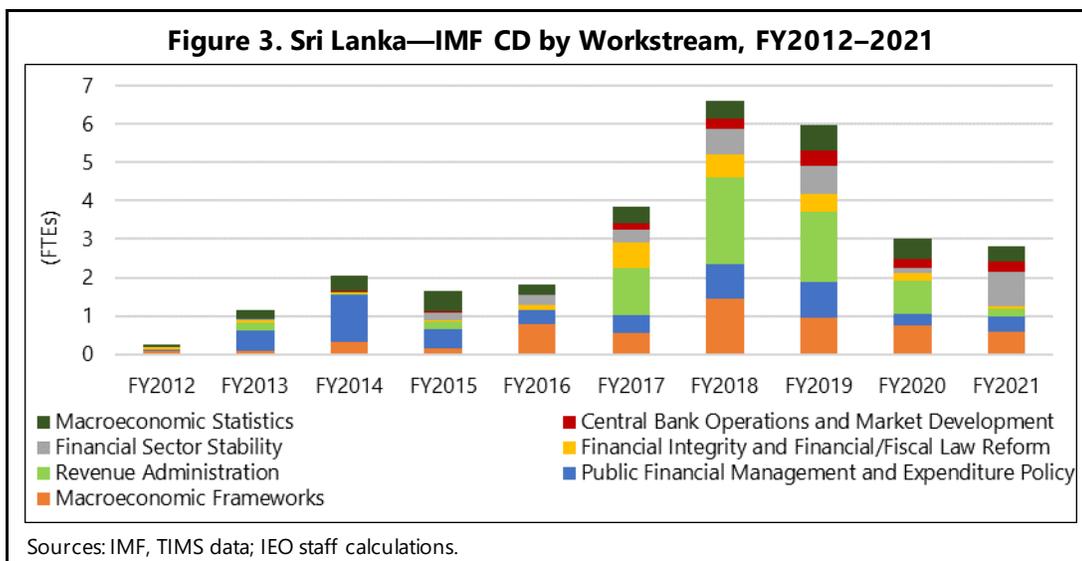
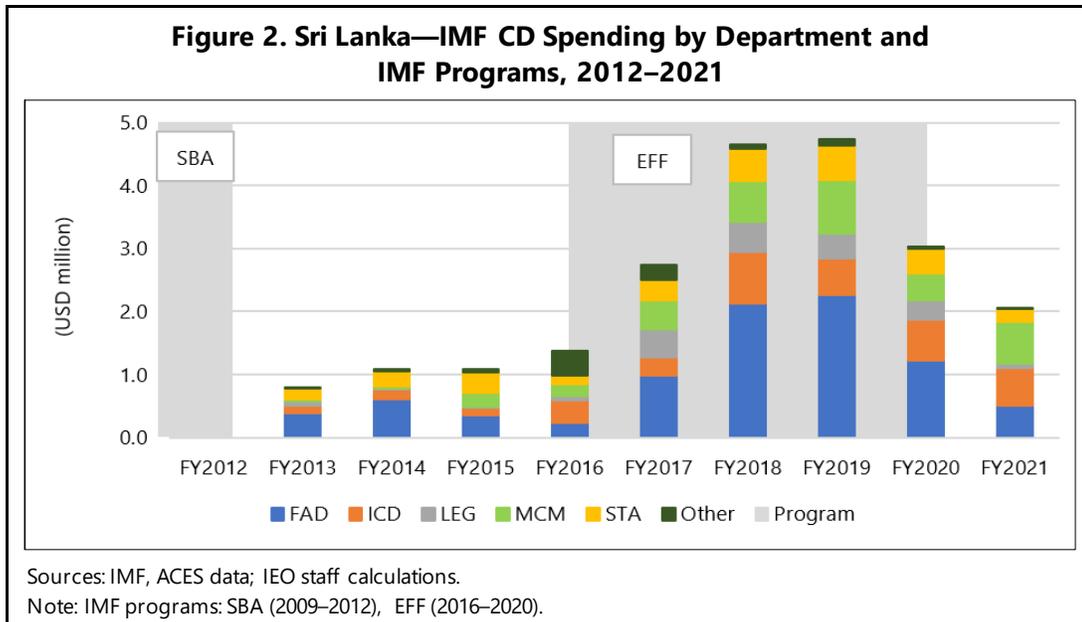
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<sup>1</sup> See IMF 2016 Article IV Consultation report.

<sup>2</sup> As measured at US\$3.2 per day in 2011 purchasing power parity (World Bank, 2021).

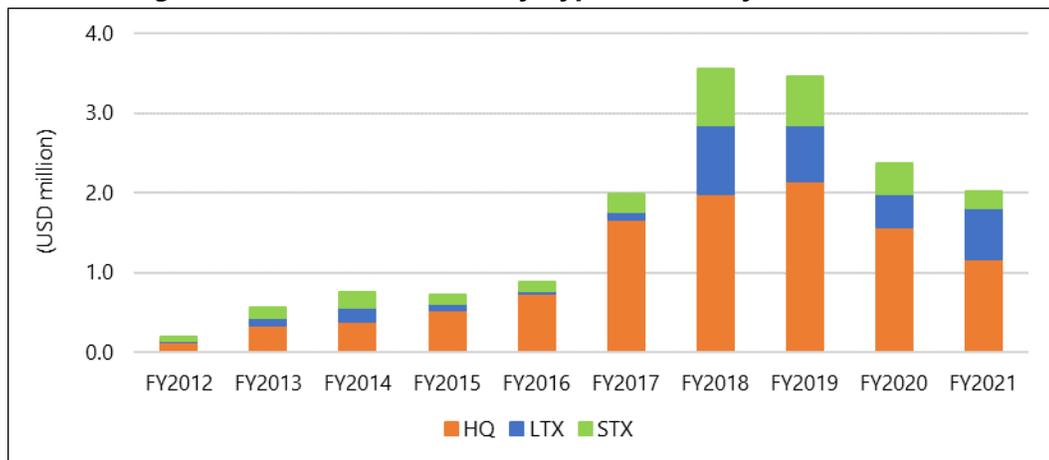


4. FAD has been by far the largest provider of IMF TA to Sri Lanka over the review period (Figure 2). In the early years, most of the assistance was in the area of public expenditure management. Since 2017, the bulk of the work was related to revenue mobilization—strengthening administration of both indirect and income taxes, and assisting with the preparation of a new Inland Revenue Act aimed at putting in place a simpler and more equitable income tax system (Figure 3). MCM provided significant assistance in 2018–2019, through its FSSR, help to design amendments to the central bank law, and also input to the roadmap for moving towards an inflation targeting framework and a more flexible exchange rate system. ICD also provided significant training in macroeconomic modeling to provide analytical input to the conduct of monetary policy.



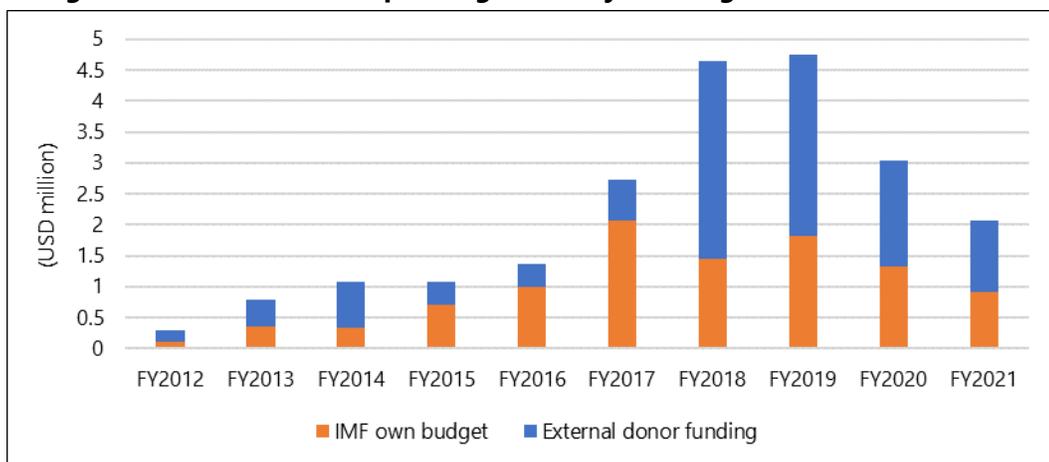
5. IMF CD delivery to Sri Lanka has largely been provided by staff from headquarters together with STXs and LTXs (Figure 4 and Annex I). In 2020, a LTX resident advisor was appointed to help the central bank strengthen macro-prudential supervision and regulation, but his arrival in Sri Lanka was delayed until the end of the year due to the pandemic and associated travel restrictions.

6. In the early part of the last decade, the bulk of CD to Sri Lanka was financed by Japanese donor funds (Figure 5). In 2015–2016, the IMF’s internal resources provided the bulk of financing. Since then, SARTTAC resources, provided by its members together with its development partners, have played a key role. Topical trust funds have also supported TA in the areas of revenue mobilization and financial stability.

**Figure 4. Sri Lanka—IMF CD by Type of Delivery, FY2012–2021**

Sources: IMF, ACES data; IEO staff calculations.

Note: Spending data excludes non-personnel (NP) costs, which include, among others, travel expenses.

**Figure 5. Sri Lanka—IMF Spending on CD by Funding Source, FY2012–2021**

Sources: IMF, ACES data; IEO staff calculations.

## II. CD ENGAGEMENT

### A. Strategy, Prioritization, and Allocation

7. IMF CD to Sri Lanka over the past decade constituted an effort to help the authorities deal with significant and persistent short-term crisis needs as well as a response to longer-term capacity building demands. Prior to 2015, the mix of CD that was delivered was largely driven by the views of the authorities, who were particularly proactive in the fiscal area. While staff developed a TA agenda following the breakdown of the program discussions in 2012, it does not appear to have been fully integrated with the IMF's surveillance process. TA was delivered on important policy issues such as revenue mobilization, public financial management, and energy tariff adjustments; this assistance was demand driven and featured strong ownership of the

authorities. In addition, STA undertook a host of activities to help strengthen Sri Lanka's statistics in a range of areas—balance of payments, national accounts and prices, and government finances. At the same time, the authorities occasionally did not take advantage of Fund expertise in other important areas—e.g., pension reform—as they chose to pursue such reforms independently.

8. The period since Sri Lanka's Extended Fund Facility (EFF) Arrangement was approved in 2016 entailed a comprehensive CD strategy linked with the IMF program, and thereby with surveillance priorities as well. The mix of CD was developed in the context of dialogue with the authorities during program discussions, and thus in principle incorporated the views of the authorities. In a number of areas, ownership was strong during the program, such as in strengthening revenue mobilization through a new Inland Revenue Act, and moving towards an inflation targeting framework. However, in other areas ownership could be thin and limited to a small group of senior officials, and in a number of cases could not overcome political obstacles. For example, certain reforms to be implemented in the context of a new fiscal rules framework and a new central bank law were derailed by changes in government. There have also been reversals of a number of tax reforms taken with the adoption of the new IRA in 2018.

9. With the change in government at end-2019, and then the onset of COVID-19, the focus of the government has been on short-term operational issues. The priorities for CD continued to be guided by the strategy agreed under the EFF program.<sup>3</sup> But the TA and training from the IMF that has since been provided—under the constraints imposed by the pandemic—has not been under the umbrella of a comprehensive strategy developed with the close involvement of the new government and authorities.

10. On the side of the staff, CD has become increasingly integrated in recent years with the policy priorities for Sri Lanka as identified by the area department country team, who have led the planning process within the Fund. As with other country cases, the role of the resident representative in Colombo has been critical to the integration effort. Coordination with CDDs has been generally close and effective, although FAD noted insufficient involvement at the outset of the 2016 program discussions (to be discussed further in the next section). Finally, the process has entailed the close involvement of SARTTAC, who have been plugged into the overall planning process as well as the design of specific CD projects.

## **B. Delivery**

11. Interviews held with the authorities and staff indicate that the average quality of the experts involved in providing CD to Sri Lanka was high. TA recommendations addressed the challenges faced by the economy, and generally took account of country circumstances. Discussions suggest that the pace and breadth of reforms in a couple areas related to policy commitments agreed under the 2016 EFF arrangement may have been too ambitious and rushed

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<sup>3</sup> See IMF (2019f), Annex V.

at the outset, driven by the need to achieve program targets. But this appears to have been related to insufficient involvement of CDDs staff when the program was set rather than poor design of the assistance itself. In any event, such issues did not appear to pertain to CD on more technical matters—such as assistance on monetary and exchange market operations and statistics. The authorities expressed satisfaction that for the central bank in particular, the reforms were well-tailored for Sri Lanka and recommendations were adjusted as warranted to fit circumstances.

12. As noted above, initial commitments agreed by the authorities at the outset of the 2016 EFF related to the design and implementation of a new Inland Revenue Act and improvements to VAT administration appear to have been unrealistic. However, CDDs staff were requested to provide TA on policy design and implementation plans several months after the beginning of the arrangement. From that point on, extensive training and hands on assistance was provided to relevant authorities—the October 2019 staff report for the 6<sup>th</sup> EFF program review lists 30 missions to Sri Lanka in the areas of tax policy and tax administration from May 2017 to September 2019—and the breadth and schedule of reforms were adjusted to be more in line with institutional capacity.<sup>4</sup>

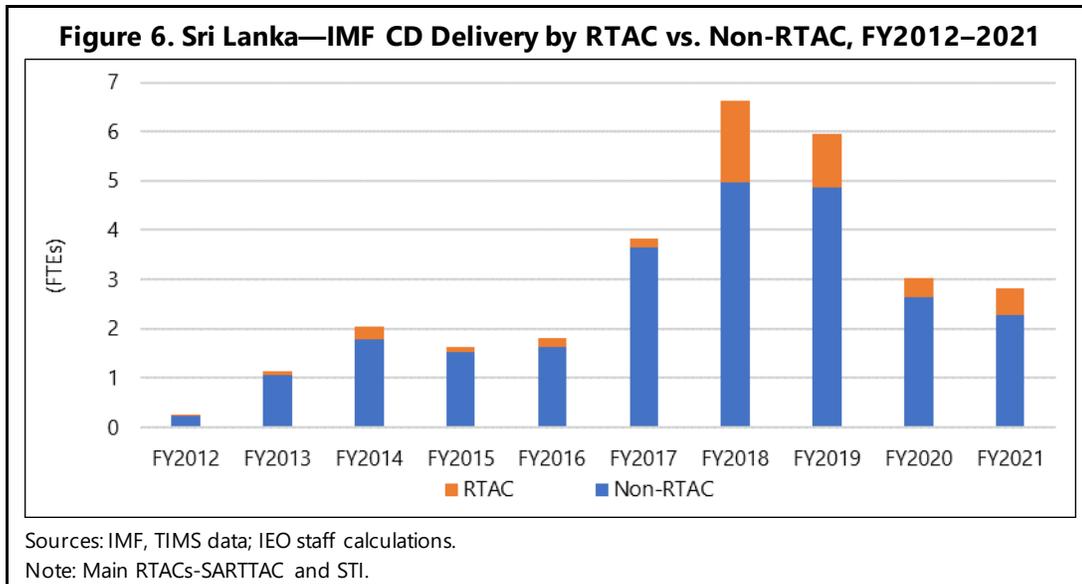
13. The authorities indicated that the significant assistance provided by the IMF to the central bank in the areas of monetary and exchange rate policy as well as financial sector regulation and supervision was well tailored to Sri Lanka and was very helpful in enhancing capacity. As in the case of Cambodia, the FSSR for Sri Lanka in 2018–2019 was a well-planned exercise, with a range of external expertise brought to bear (IMF, 2019e).

14. Up to FY2017 the extensive CD was delivered mainly by HQ staff, supported by short-term external experts (Figure 4). Since 2017, a significant role has been played by SARTTAC regional advisors, who participated in TA and also conducted a number of regional training courses (Figure 6). The authorities highlighted the positive role played by regional advisors. Nevertheless, they thought that in a number of instances, a resident advisor on the ground would have been helpful, and looked forward to contributions from a newly appointed LTX on macro-prudential issues. With regards to the use of STX, ensuring continuity was critical. In a few cases, problems in information transfer between experts had hampered effective assistance.

15. The COVID-19 pandemic severely disrupted CD activity in Sri Lanka. Several interviewees indicated that lockdowns, poor internet access and time zone differences combined to reduce the effectiveness of webinars and training courses in particular. In the event that travel restrictions were to continue for some time, some resident presence of TA experts would be desirable.

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<sup>4</sup> As described by CDDs staff. Area department country team staff agree that CD in this area included support needed to bolster implementation capacity. See Annex V of the Staff Report for the 6<sup>th</sup> Review under the EFF arrangement for a list of TA missions since May 2017.



### C. Partnerships and Coordination

16. The IMF's work on Sri Lanka featured close collaboration with the World Bank and other CD providers and partners. The country team at IMF HQ and the resident representative in Colombo communicated regularly with World Bank and Asian Development Bank counterparts, and CDDs staff also worked closely with their counterparts, especially those at the World Bank.

17. During 2016–2020, there was extensive joint CD provision in support of the 2016 EFF:

- In the area of public debt management, FAD and the Bank worked jointly to support the development of a Medium-Term Debt Strategy and the establishment of an independent debt management agency.
- In PFM, the World Bank led joint work to support a new PFM Act, and a joint Public Investment Management Assessment was conducted in 2017.
- In the financial sector, there was work led by the Bank in support of a new Banking Act, and an FSSR follow-up TA project was designed in consultation with the World Bank in 2019.

18. Staff interviews indicate that the CD work was divided quite rationally and cooperation was positive.

19. IMF TA reports on Sri Lanka are with a few exceptions unpublished (Annex I, Table AI.3). While there appears to be no formally expressed opposition by the authorities to publication, the lack of publication appears to reflect the sensitive nature of many of the reports, prepared in the context of IMF program conditionality. Finally, there appears to be limited use of peer-to-peer

learning opportunities, with the exception of insights provided in the context of regional training courses conducted by SARTTAC.

#### **D. Impact and Effectiveness**

20. IMF CD activities have been well regarded and appreciated in Sri Lanka. In many areas, IMF CD has been effective in supporting Sri Lanka's efforts to secure financial stability and build stronger macroeconomic institutions and policy making capacity. In several areas, however, results have been mixed, particularly where CD was mainly linked to program conditionality and where ownership dissipated with political and personnel changes (and the termination of the program).

21. During 2016–2020, guided by Fund-wide strategic objectives, CD activities in Sri Lanka were closely integrated with the key objectives of the EFF-supported policy program. The IMF staff report for the Sixth Review under the EFF details achieved outcomes following TA and training engagements in a full range of policy areas.<sup>5</sup> To note a few:

- In tax policy, VAT amendments in 2016 and 2018 helped to boost VAT collections, a new Internal Revenue Act (IRA) was launched in 2018, and in 2019 cabinet approved a plan to rationalize Sri Lanka's tariff structure. A host of steps to improve tax administration were also implemented.
- To strengthen medium-term fiscal management, the Cabinet of the government then in office approved a new fiscal rule framework in 2019.
- With regards to monetary and exchange rate policy, the central bank's roadmap to inflation targeting and a flexible exchange rate regime was adopted in 2017, the central bank developed a model-based forecasting and policy analysis system to inform policy formulation, and a new Central Bank Act to institutionalize the modernization of monetary policy and as recognize the central bank as the macro-prudential authority was submitted by the then Minister of Finance in 2019.
- With regards to strengthening statistics, a national CPI was released in 2018, plans were adopted to rebase national accounts, and steps were taken to transition to fiscal reporting consistent with Government Finance Statistics Manual (GFSM) 2014.

22. In a number of important policy areas, however, reforms in line with CD recommendations under the program were not widely owned, and were ultimately not implemented or reversed following the change in government in 2020. A new fiscal rules framework was not adopted, and planned legislation to introduce a new central bank act has been scrapped. The change in government also led to reversals in tax policy and administration

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<sup>5</sup> IMF (2019f).

reforms. A number of provisions under the 2018 IRA were retracted, and VAT exemptions were reinstated along with wide-ranging rate cuts. Aside from the issue of fiscal policy stance, structural reforms to the tax policy and administration frameworks do not appear to have been widely owned by counterparts.

23. Finally, on the use of mechanisms to manage results and enhance effectiveness, clearly the commitments under the EFF arrangement provided the timetable and expected outcomes. At a more technical level, the application of RBM methodologies appears to still be a work in progress, with only a small proportion of project objectives and outcomes having been rated (Annex I, Figure AI.1). MCM staff report that RBM is in place for all projects and that expected milestones are discussed with the authorities *ex ante*, with flexibility to make adjustments if the authorities are not ready to implement in line with the suggested plan. At the same time, there appears to be little awareness or use of RBM at the level of the IMF country team, possibly hindering efforts at CD integration and follow-up assistance with implementation.

### III. OVERALL ASSESSMENT

24. Sri Lanka was a significant recipient of IMF CD over the 2012–2020 review period, with CD delivery ramped up sharply under the 2016–2019 EFF arrangement. During the early part of the decade, CD was demand-driven, though not allocated in the context of a comprehensive framework of policy priorities. Subsequently, CD delivery was closely integrated with the achievement of key policy objectives of the EFF-supported program, and covered both short-term crisis management policies as well as longer-term institution building needs. The scope and nature of CD delivery thus reflected the views of the authorities, but in a number of cases appears to have been dominated by the need for compliance with conditionality, and may not have been deep enough to ensure lasting results when political circumstances changed.

25. Notwithstanding such ownership issues, official counterparts highly valued the expertise embodied in the CD that was delivered. Collaboration with other providers were well-coordinated with an effective division of labor. The dialogue between CD experts and country officials was constructive, and TA recommendations were generally well suited to the circumstances on the ground at the time, with flexibility shown to address implementation delays when they materialized. Assistance and training to build capacity were acknowledged; the regional advisors located in SARTTAC as well as the IMF's resident representatives in Colombo were particularly helpful. With the effectiveness of virtual CD rather limited in Sri Lanka's case, resources permitting it would be desirable to enhance SARTTAC's role as well as consider the placement of long-term resident advisors where ongoing capacity building and training were particularly important to the successful implementation of CD recommendations.

26. Sri Lanka's experience highlights the susceptibility of implementation of CD recommendations to political circumstances. And while close integration with EFF objectives and conditionality meant that CD could play an important supportive role to success of the program, it also increased the risk that ownership would dissipate with regime change or termination of

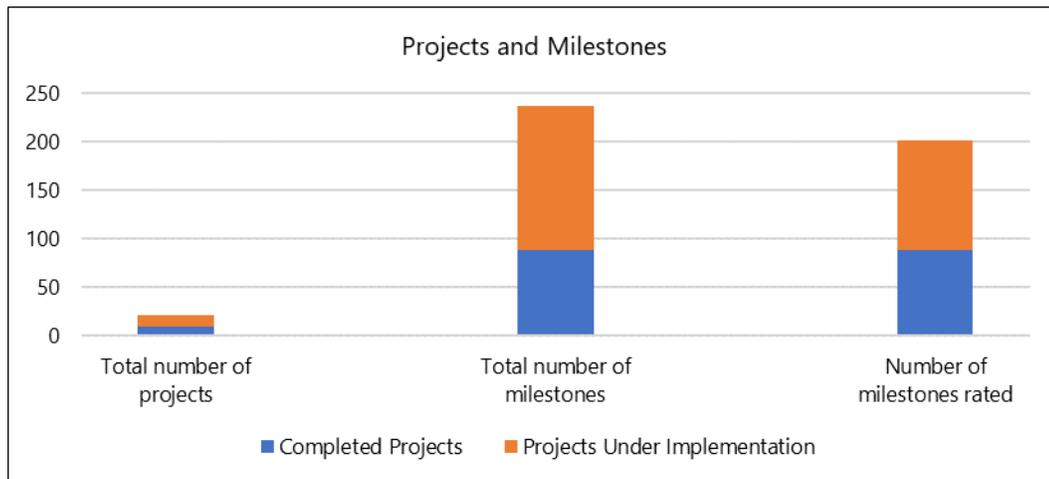
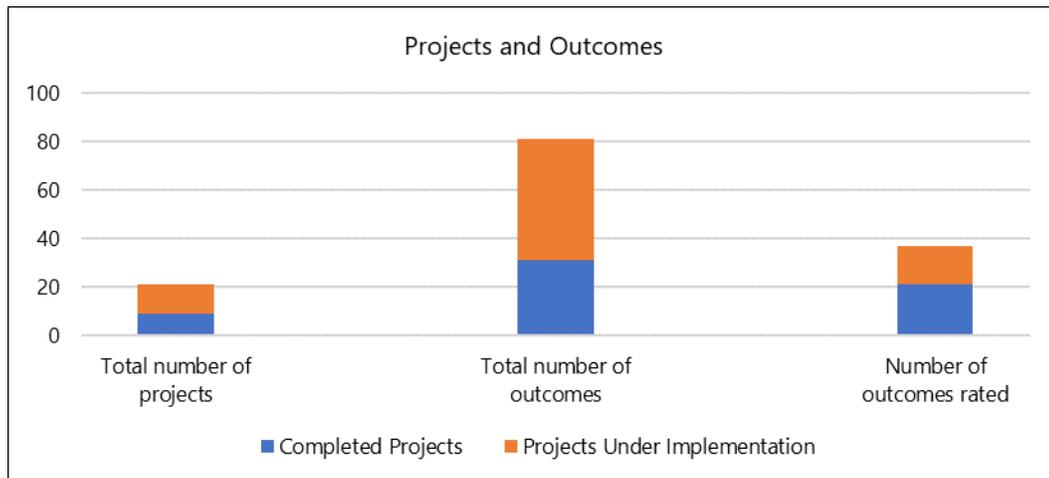
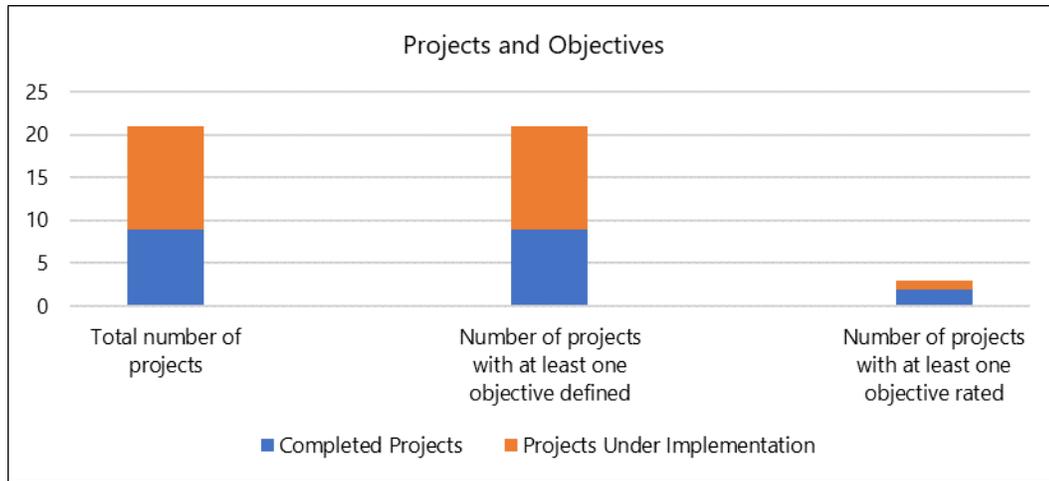
the arrangement. It is inevitable, particularly in economies where policy frameworks, traditions, and institutions are still developing, that IMF CD recommendations face the risk of incomplete implementation, reversals or non-acceptance. And, of course, it is any country's sovereign right to change course.

27. That said, steps could be considered to further embed ownership and mitigate such risks, particularly given the need to prioritize limited financial and human resources. Some actions to be considered are:

- In formulating country CD strategies, ex post assessments of previous delivery efforts should be an integral part of the planning process. In areas with significant prior delivery, explicit strategies should be formulated to minimize the risks and cost of weak implementation.
- In areas of weak past implementation, focus may be shifted, at least initially, to building skills and training, thereby strengthening the likelihood of future success in framework or process reforms. Such CD could be delivered independently of any program conditionality and its impact would be sustained beyond the life of a program engagement.
- CD efforts should be carefully calibrated not only relative to implementation capacity but also to the depth of ownership. In retrospect, a number of stakeholders acknowledged that some reform efforts and CD recommendations were too broad and ambitious in scope.
- And last but not least, together with the authorities, appropriate outreach efforts should be made to build wide ownership. Particularly with regards to important reforms to institutional or policy frameworks (such as the fiscal rules framework or the central bank act), outreach efforts to maximize the chances of broad understanding and acceptance would be desirable.

## ANNEX I. CD ACTIVITIES FOR SRI LANKA

**Figure AI.1. Sri Lanka—Results Based Management Data on Projects, Objectives, Outcomes, and Milestones**



Sources: IMF, RBM data; IEO staff calculations.

**Table AI.1. Sri Lanka—Number of Missions, 2012–2020**

Year	FAD	ICD	LEG	MCM	RES	STA	Others	Total
2012	1	0	2	0	0	1	0	4
2013	6	0	1	1	0	4	0	12
2014	11	0	0	0	0	5	1	17
2015	6	0	0	1	0	8	0	15
2016	2	2	2	1	3	2	3	15
2017	18	2	9	2	0	4	1	36
2018	27	5	11	5	0	3	2	53
2019	18	3	8	10	0	4	0	43
2020	10	3	4	1	0	7	1	26
Total	99	15	37	21	3	38	8	221

Sources: IMF, TIMS data; IEO staff calculations.

**Table AI.2. Sri Lanka—Resident Advisors, 2020–2021**

Host institution	CDD	CD topic/workstream	Start date	End date
Central Bank	MCM	Macprudential Policy and Stress Testing Advisor (Year 1)	8/1/2020	7/31/2021

Source: IMF, Fiscal Affairs Department, and Monetary and Capital Markets Department.

**Table AI.3. Sri Lanka—List of TA Reports, 2012–2020**

	FAD	MCM	STA	LEG	SARTTAC	Total	Of which		
							Available within IMF	Available but confidential	Published
2012	2	0	2	0	0	4	2	0	0
2013	1	0	4	0	0	5	0	1	0
2014	1	0	2	0	0	3	1	0	0
2015	2	0	6	0	0	8	2	0	0
2016	1	3	3	0	0	7	4	0	0
2017	3	4	2	2	1	12	8	1	0
2018	6	1	4	1	0	12	1	0	1
2019	4	3	7	1	0	15	7	1	0
2020	0	1	2	0	0	3	1	0	0
Total	20	12	32	4	1	69	26	3	1

Source: IMF, Institutional Repository.

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