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The IMF's Exceptional Access Policy in the 2020 Stand-By Arrangement and Rapid Financing Instrument for the Arab Republic of Egypt

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ABBREVIATIONS

BOP	Balance of Payments
EAP	Exceptional Access Policy
EPE	Ex Post Evaluation
GCC	Gulf Cooperation Countries
RFI	Rapid Financing Instrument
SBA	Stand-By Arrangement
EA	Exceptional Access
GDP	Gross Domestic Product
EFF	Extended Fund Facility
HP Tool	High Probability Tool
MAC DSA	IMF Debt Sustainability Framework for Market Access Countries
MAC SRDSF	Sovereign Risk and Debt Sustainability Framework for Market Access Countries
NIB	National Investment Bank
PCI	Policy Coordination Instrument

EXECUTIVE SUMMARY

The IMF supported Egypt's response to the COVID-19 pandemic with a combination of a US$2.8 billion Rapid Financing Instrument (RFI)—approved by the Board on May 11, 2020—and a 12-month, US$5.2 billion Stand-By Arrangement (SBA)—approved on June 26, 2020. Both were made possible by and met the exceptional access policy (EAP). Their overall objective was to protect macroeconomic stability at a time of high external and budget financing needs and extreme uncertainty. The Fund and authorities envisaged that exceptional access (EA) to Fund resources would stem net capital outflows, catalyze further external financing, and help support economic activity and social assistance.

Policy conditionality was limited. The SBA focused on providing short-term support in an emergency situation—it involved no adjustment and little structural reform in the context of the pandemic. RFIs do not carry ex post conditionality.

The RFI and the SBA, facilitated by the Exceptional Access Policy (EAP), were successful in meeting immediate needs. Net outflows were arrested and turned to inflows, growth and social stability were supported, and the worst outcomes were avoided. The economy proved more resilient than envisaged in program projections, which proved pessimistic.

While it addressed immediate needs, the package may have been a "missed opportunity" to address structural problems. The short period of the SBA—at the lower end for a typical SBA—and the consequent relative lack of macroeconomic and structural policy changes entailed leaving Egypt with vulnerabilities in the post-program period.

The EAP provided a useful framework but its application in Egypt also pointed to some broader lessons for the policy. The EAP was considered useful for carefully thinking through Egypt's financing needs, debt sustainability, market access, and prospects for program success and for considered decision making by the Fund. While the EAP was met during the program, the Fund was left with residual risks in the subsequent period.

Key findings and conclusions of this paper with respect to the strategic value and performance of the EAP and its components (criteria, procedures, ex post evaluation) are as follows.

With regard to the first criterion on exceptional balance of payment (BOP) pressures:

- The EAP could more systematically incorporate a mechanism to deal with the materialization of upside risks that reduce BOP needs during the course of the arrangement.

- Given that exceptional access implies large IMF repurchases in the future, decisions on access levels should take careful account of future repayment capacity and of the implications of future repurchases for the member's BOP. Decisions on access levels should be mindful of the need to reduce the risks of prolonged reliance on Fund support. A short program with EA may imply bunching of large subsequent repurchases.

Regarding debt sustainability assessments (the EAP second criterion):

- It was hard for staff to judge debt as "unsustainable" given that the government had recent market access and no arrears. Declaring debt "unsustainable" would have required debt restructuring, with risks of disruption to market access, currency instability, and potentially protracted and costly negotiations.

On the third criterion (market access):

- The Fund's lack of a standard methodology to assess prospects for market access poses a problem. The criterion was deemed met based on Egypt's latest issuances of Eurobonds (a backward-looking assessment).

In terms of the fourth criterion (prospects for program success):

- More political economy analysis would be useful to judge *ex ante* the authorities' political and institutional capacity to meet program commitments. That would also help broader enterprise risk management. In Egypt's case, the Fund could have benefited by building its own capacity or partnering more closely with specialized institutions to strengthen relevant aspects of the design, implementation, and follow-up of structural reforms.

On the enhanced EAP decision-making procedures:

- When EA is due to an emergency, there may be little time to follow closely the EAP's requirements and expectations for enhanced Board consultations. In Egypt's RFI and SBA the requirements were followed, but additional informal consultations did not take place.
- The IMF staff did respond promptly to the authorities' request for support, without compromising technical quality and while adapting to an unprecedented operational form of remote work.

The ex post evaluation (EPE) of Egypt's SBA was delivered on time. (EPEs are not required for RFIs.) It mainly described outcomes (the "whats") rather than the reasons for those outcomes (the "whys"), which could have provided useful additional lessons. It sought views from a relatively narrow set of external stakeholders.

I. INTRODUCTION AND METHODOLOGY

1. **This paper evaluates the application of the IMF's Exceptional Access Policy (EAP) to Egypt's 2020 Rapid Financing Instrument (RFI) and Stand-By Arrangement (SBA).** Its principal focus is the performance of the *policy*, not the performance of the *program*. Did the EAP help the program achieve its objectives? How necessary was exceptional access (EA)? How well was it decided upon and delivered? What lessons can be drawn that could be useful beyond the Egyptian context? The answers to these questions help to provide country-specific inputs for the evaluation of the EAP being carried out by the Fund's Independent Evaluation Office (IEO).[1, 2]

2. **At the outset, it is important to note that the EAP does not limit how much a government can borrow from the IMF.** Rather, it was created in 2002 as an additional layer of risk management so countries can borrow amounts in excess of their normal limits to IMF resources (that is, have "exceptional access") when appropriate and with adequate safeguards.[3] For an IMF arrangement to commit more than 145 percent of the member's quota on an annual basis or 435 percent on a cumulative basis, four technical criteria need to be met, the Executive Board needs to be consulted early, and an ex post evaluation needs to be produced.[4, 5] Those four criteria relate to the existence of an *actual* or *potential* balance of payments (BOP) need in excess of normal access limits; public debt sustainability; prospects that the government will have market access *when repayments to the Fund come due*; and *reasonably strong* prospects of program success. The italicized qualifiers matter. They were decisive in granting exceptional access (EA) to Egypt.

3. **It is important to acknowledge that this paper benefits from hindsight.** As Figure 1 shows, chronology plays a central role in the country case presented here—what was known when. The information available and the sense of urgency in 2020 were very different from today, involving extraordinary uncertainty and a need for prompt action. The COVID-19 pandemic had broken out in March 2020. It was spreading rampantly, with growing fatalities and no prospects yet of the vaccine that would only arrive in December 2020.[6] The initial blow to the Egyptian economy had been dramatic. Its growth was cut in half and the country's main sources of foreign currency were drying out. Tourism came to a virtual standstill as airports were shut down.

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[1] See IEO (2023a).

[2] The findings and arguments presented in this paper are based on published and internal IMF documents, cited papers and sources of country data, and 58 interviews with current and former institutional staff, government officials, officers of multilateral organizations, bilateral donors, and Egyptian and foreign financiers and investors. The interviews took place in Washington and in Cairo between October 2023 and February 2024.

[3] See Abrams and Arora (2024) for a description of the EAP and a discussion of its rationale and evolution.

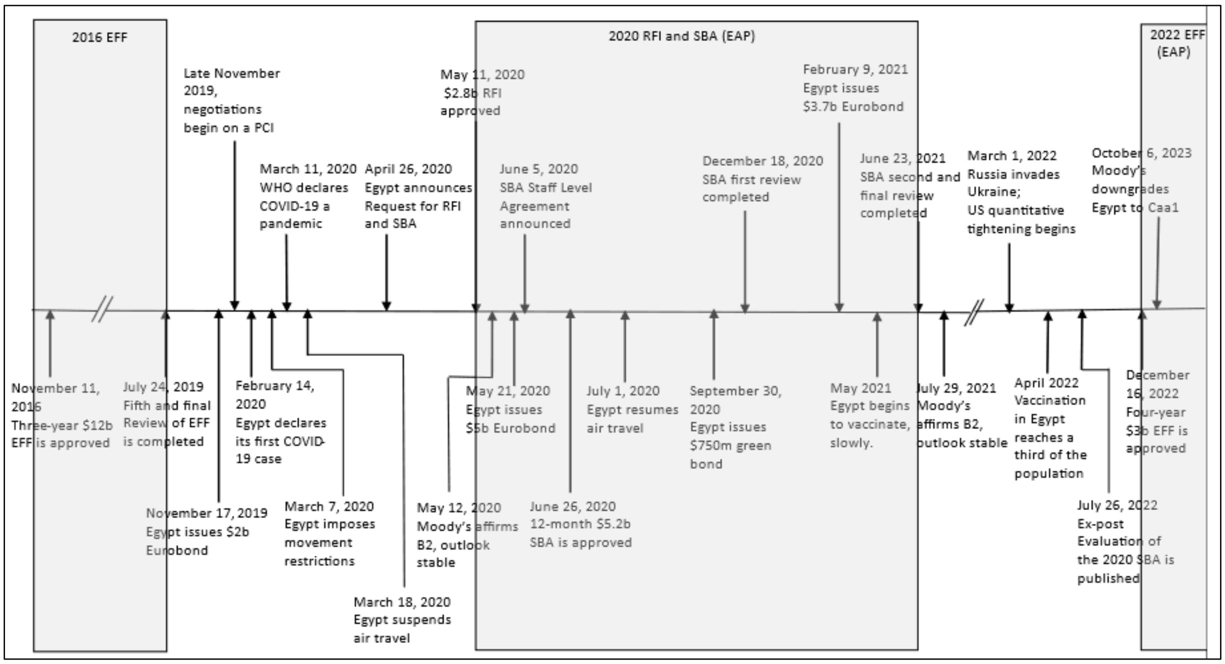
[4] Those thresholds were temporarily raised (to 200 percent and 600 percent, respectively) for a year in March 2023, in view of the various global crises, and later continued through end-2024.

[5] Note that EAP applies to funding from the General Resource Account (GRA). Exceptional funding from the Poverty Reduction and Growth Trust (PRGT) has separate but equivalent rules.

[6] Through September 2023, the World Health Organization reported 516,023 confirmed cases and 24,830 deaths due to COVID-19 in Egypt. Available at https://covid19.who.int/region/emro/country/eg.

Remittances and Suez Canal revenues were expected to fall drastically over the subsequent 12 months—by as much as a quarter and 15 percent, respectively. The outlook would be worse the longer global value chains were disrupted. The projected external financing gap went from zero right before COVID-19 to almost 10 percent of gross domestic product (GDP) right after. Meanwhile, fiscal revenues were falling with the lockdown of economic activity, and pandemic-related expenditures were ballooning.

Figure 1. The Timeline Around Egypt's 2020 SBA



Source: Authors.

4. **It was then natural—and sensible—to plan a baseline macroeconomic framework where the crisis would last for a year.** That meant projecting exceedingly large financing gaps in fiscal years 2019/2020 and 2020/2021.[7] To its credit, the IMF led the way in filling those gaps. It deployed two instruments in quick succession. First, a US$2.8 billion RFI was disbursed in May 2020. This brought Egypt to exceed the limit for normal *cumulative* access. Second, a 12-month, US$5.2 billion SBA was approved in June and implied that Egypt would also exceed the normal *annual* access limit. Both the RFI and the SBA thus triggered the EAP.

5. **The idea behind that two-pronged funding strategy was to provide enough comfort for other creditors—multilateral, bilateral, and commercial—to follow suit.** This would preserve macroeconomic stability while allowing the government to pay for targeted emergency support to people and enterprises. Given the pandemic circumstances, the program did not envisage fiscal or monetary tightening, nor significant structural reforms. The strategy

[7] Egypt's fiscal year runs through June 30.

carried risks, for both Egypt and the Fund, especially if implementation slipped, if the Fund's debt sustainability assessments proved sanguine, and if the pandemic extended beyond 2021. But, given the situation at the time when decisions were made, the wait-and-see alternative of not proceeding with a program was riskier.

6. **Did the application of the EAP to the RFI and the SBA work? It did, but not for the expected reasons.** While the IMF's support did provide reassurance to financiers, it was the resilience of the economy and the speed of its recovery that surpassed projections. The outlook on which the SBA was conceived, and for which the EAP was invoked, turned out to be too pessimistic. By the first review, it was clear that private capital—albeit short term—was returning. But there was no *built-in* way in the program to roll back financial access in view of the stronger-than-expected BOP. There was no leverage to address policy misalignments either—among others, in the implementation of the foreign-exchange regime, the fiscal stance, or the distorting role of the off-budget public sector. That left the Egyptian economy with deep-seated vulnerabilities, which surfaced after the SBA.

7. **The rest of the paper is organized in four sections.** Section II describes the context in which the RFI and SBA were designed, decided, and implemented. The role that the 2016 Extended Fund Facility (EFF) and its achievements played in the emergency operation and in the relationship with the authorities will be highlighted. Section III reviews the use of the EAP to make the RFI and SBA possible. A detailed analysis of how various criteria and procedural requirements were met—or not—and how they served—or not—the objectives of the financing package is presented. This allows for the study of the actual interplay between program design and EAP: to what extent the latter was leveraged to achieve of objectives of the former. The bottom-line issue of impact follows in Section IV: did the EAP itself make a difference? At what cost? Finally, lessons are distilled in Section V, not as recommendations, but as inputs to future use—or reform—of the EAP.

II. CONTEXT: AN RFI AND AN SBA IN-BETWEEN TWO EFFS

8. **Egypt has a long history of borrowing from the IMF.** Its first SBA dates back to 1962.[8] The country has since had eleven more programs, the last three of which are depicted in the timeline of Figure 1. The largest, and arguably the most impactful, being the EFF approved in 2016. This three-year arrangement, which came after two decades of no financial relationship, involved US$12 billion in disbursements. It took Egypt's cumulative use of quota from zero to 422 percent—that is, just under the limit for EAP.

9. **The 2016 EFF provided useful support.** By the time it concluded in 2019, the economy was growing at almost 6 percent per annum, inflation was in single digits (from some 30 percent per annum three years earlier), the public debt burden had declined by 20 percentage points to

[8] See "Egypt: History of Lending Commitments" at www.imf.org/external/np/fin/tad/extarr2.aspx?memberKey1=275&date1key=2021-02-28.

some 80 percent of GDP and, while still relatively large, budget imbalances were half what they were at the beginning of the program and falling. Significant structural reforms were implemented or launched—like the elimination of fuel subsidies, reinforcing social protection through direct cash transfers to the most vulnerable, and the strengthening of the governance of the National Investment Bank (NIB). The impression that the government owned the agenda prevailed among both multilaterals and investors. Egypt was able to tap international markets—helped by the global environment of very low interest rates. The EFF left some much-needed reforms pending, among others, in raising tax collection, inflation targeting, privatizing state-owned enterprises, allocating industrial land, giving more space to the private sector in public procurement, and allowing the exchange rate to fluctuate freely. But the overall movement was in the right direction.

10. **To support that movement, and in the absence of a financing gap, the government and the IMF began, in late 2019, to negotiate a Policy Coordination Instrument (PCI).** The negotiations covered an agenda of structural measures to be implemented over three years and for which the Fund would provide non-financial support through continuous monitoring, evaluation, and technical assistance, directly or by mobilizing other institutions. The intention was to reassure financiers and investors that Egypt's policy framework and growth prospect were solid.

11. **The outbreak of COVID-19 in March 2020 was a significant disruption.** The seriousness of the crisis soon became apparent and IMF staff soon agreed with the authorities that ample financial assistance was urgently required, both for the fiscal budget and for the projected gap in the balance of payments (BOP)—capital outflows were large, rapid, and growing. In response, the notion of the PCI was dropped and, in its stead, an RFI was approved on May 11 for US$2.8 billion (100 percent of quota), followed by an SBA on June 26 for US$5.2 billion (185 percent of quota).

12. **The main, explicit objective of the RFI and SBA was to protect the stability of the economy in the face of the fiscal and balance of payments shocks that the pandemic had caused.** This would be achieved through an infusion of liquidity big enough to build confidence and keep funding from other creditors and donors coming. Structural reforms would be pursued but were less of a priority in the short term. The macroeconomic stability to be preserved was, in no small measure, the result of the 2016 EFF.

13. **By design, the SBA carried a macro-policy mix that was accommodative of the realities.** RFIs carry no ex post conditionality. The quantitative performance criteria and indicative targets set out at time of approval (June 2020) called for a *decline* in the primary fiscal surplus by 1 percent of GDP—with a floor for social expenditure—a backloaded increase in the central bank's foreign currency reserves worth 60 percent of the SBA's disbursements, and no

accumulation of arrears—something Egypt was already observing.[9] The authorities were in principle committed to exchange rate flexibility, although in practice they had defended the Egyptian pound since the start of the crisis, contributing to a fall in reserves.

14. **On the structural side, the SBA's benchmarks picked up where the 2016 EFF left off and the PCI would have set out from, but with more focus on process than results.** Policymakers' time and attention were absorbed by the pandemic. The matrix of actions was about developing a strategic plan for the NIB, submitting laws to Parliament on public financial management and market competition, streamlining of customs procedures, updating the public debt management and fiscal revenue strategies, and doing a public expenditure review. Those actions were all completed. In addition, the SBA allowed for measures that, in normal times, would have been considered distortionary—from subsidizing electricity and gas in selected industries to financial support to aviation and tourism. That was estimated to cost three quarters of one percent of GDP.

15. **Given the pandemic circumstances, the SBA was not unusual in terms of its limited conditionality**. A recent IEO evaluation of *The IMF's Emergency Response to the COVID-19 Pandemic* (IEO, 2023b) found that, in the early months of the crisis, programs with loosening fiscal stances, "stimulative" monetary policy, no or scaled-back prior actions, and "benefit of the doubt" about debt sustainability were the norm. This entailed increased risk for the institution, but one that was outweighed by the reputational risk of not responding. That calculation would come to define the Egyptian case.

16. **The SBA was successfully completed.** Both of its reviews were done on time and without waivers, and its funding was released. That was expected: the operation's performance criteria and indicative targets were not demanding and its structural content was light. Most importantly, macroeconomic stability was maintained. Social expenditures were increased, especially health-related ones, albeit with mixed outcomes during implementation.

17. **But the stability that the RFI and the SBA helped gain masked vulnerabilities.** The fiscal relaxation accommodated during the pandemic was not reversed, pushing public debt onto a rising path. A de facto peg of the exchange rate exposed the central bank's foreign-currency reserves to sudden capital outflows. Credit ratings did not improve and remained stuck below investment grade. The structural reforms that would rein in the off-budget public sector and unleash private-sector-led growth were still on the drawing board.

18. **It did not take long for those vulnerabilities to be tested.** In March 2022, two shocks hit Egypt in quick succession: first, the jump in food and fuel prices that followed Russia's invasion of Ukraine; second, a rapid increase in policy interest rates in advanced economies.

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[9] During the pandemic, social spending floors became a practice in IMF programs, especially those funded out of the Poverty Reduction and Growth Trust (PRGT). Their formalization, however, dates back to 2019 with the publication of the policy paper on a strategy for IMF engagement on social spending (IMF, 2019a).

III. EVALUATION OF IMF PERFORMANCE: WAS EA THE RIGHT THING TO DO? WAS IT DONE RIGHT?

19. **Given the extraordinary uncertainty when the pandemic broke out, it seemed sensible to plan for the worst.** The Egyptian authorities and the IMF staff did that with large upfront support in the form of the 2020 RFI and SBA. The strategic objective of the tandem was to stem the immediate crisis and to catalyze other financing. Structural reform was less of an immediate priority. That seems to have been a well-founded decision, given the information at hand. The speed with which the operations were put together speaks of the constructive relationship between the government and the Fund—perhaps a byproduct of the successful 2016 EFF.

20. **Based on a baseline scenario of a year-long disruption to all economic activities, and its implication for the BOP, the total volume of IMF financing judged necessary to achieve the strategic objective was US$8 billion**. For that, EA had to be invoked as the 2016 EFF had left Egypt's outstanding Fund credit 13 percent of quota shy of the *cumulative* access limit (435 percent). Any significant funding was bound to trigger the EAP. Thus, the RFI (100 percent of quota) caused the cumulative access limit to be exceeded, and the subsequent SBA (185 percent) took it even further.[10, 11] A key question was how large the arrangement should be. The emergency and uncertainty suggested a need for a large response. While larger disbursements would mean high surcharges and repayment obligations, the more pressing considerations for the government were to deal with the crisis at hand.[12]

21. **With the EAP triggered, a sequence of risk-mitigation steps was required**. They had to do with the EAP criteria, procedural governance, and ex post evaluation (EPE).

a) Meeting the EAP Criteria

22. **Both the RFI and the SBA easily met the first criterion of the EAP:** *"The member is experiencing or has the potential to experience exceptional balance of payments pressures on the current account or the capital account resulting in a need for Fund financing that cannot be met within the normal limits*."

23. **At the time of the arrangements' Board approval in mid-May and late June 2020, that is, at the end of Egypt's fiscal year 2019/20, Fund staff assessed that the damage brought about by the pandemic had already been vast, and the worst was yet to come.** A deepening deterioration of the external accounts was the baseline scenario for fiscal year

[10] For annual access, the RFI did not exceed the threshold—which is 145 percent of quota. It was the SBA that did (185 + 100 > 145).

[11] Interestingly, faced with the ballooning global crisis, in July 2020 the Board temporarily raised the annual threshold to 245 percent of quota, which would have kept Egypt's annual access "normal."

[12] Interviews with Egyptian authorities and IMF (2016).

2020/21, that is, the year the SBA would cover. This is shown in Table 1, where the key components of Egypt's BOP are presented. For example, it was thought that revenues from tourism, which had already fallen by a fifth, would fall by another three-fifths. Similar, successive, double-digit declines were projected for remittances and Suez Canal traffic. The consequence was a financing gap that was expected to go from zero to US$9 billion, and to worsen to US$12.2 billion. The potential for a lingering and worsening problem was on the cards. Recovery would not happen at least until July 2021—if it happened. The situation fitted the first criteria of the EAP.

Table 1. In June 2020, It Was Expected That The Worst Was Yet To Come
(In billions of U.S. dollars)

	2018/19 Actual	2019/20 Estimated at time of SBA's Board Approval	2020/21 Projected at time of SBA's Board Approval
Tourism	12.6	10	2.7
Suez Canal	5.7	5.2	4.9
Remittances	24.8	21.6	18.7
Current Account Balance	-10.9	-14.8	-16.2
FDI (net)	7.9	8	5.5
Portfolio Flows	4.1	-7.5	3.5
Net Foreign Assets of Local Commercial Banks	2.2	-4	-6.3
External Financing Gap	0	-9.2	-12.2

Source: IMF (2020a).

24. **The authorities' attempt at keeping the nominal exchange rate stable was straining not just the BOP but also the banking system**. The central bank was defending the pound with its reserves, which it then partly replenished by drawing down on foreign-currency deposits that it held in local commercial banks.[13] The RFI and SBA requests did not dwell on banking sector withdrawals or currency sales. It could have been because the data cut-off for the "financial soundness indicators" presented at the time was end–2019, before the pandemic started. The last FSAP dated back to 2018. Meanwhile, the policy dialogue on banking sector issues was about undoing as soon as feasible the pandemic-related interventions like debt moratoria and subsidized lending by the central bank. Any discussion of open net foreign currency positions at individual banks was subsumed into a general commitment to monitor compliance with regulatory ceilings—a commitment reflected in the SBA's Memorandum of Economic and Financial Policies.[14]

[13] While market intervention data is not published, the deposit withdrawal between March and May 2020—the three months before the SBA's approval—amounted to a sizable US$7 billion. Reserves fell by US$9.5 billion in the same period.

[14] There was also an impression among the IMF staff that the banking system was not going to be destabilized by the pandemic as most of its assets were Treasury bills, and non-performing loans would not be an issue because credit to the private sector was relatively small. Up-to-date bank-level data to confirm that impression was not available before the SBA was approved.

25. **These interventions were planned to be temporary.** The SBA planned for them to cease at the outset of the program and incorporated an accumulation of Net International Reserves as a performance criterion of US$3.3 billion by the time of Second Review. But the program did not put a limit to the draw-down of foreign-currency deposits, nor did it define the criterion based on the aggregate net foreign assets of the central bank.[15] Nonetheless, it projected that Net Foreign Assets (NFA) of commercial banks would fall by US$2.2 billion in the first year and continue falling thereafter.

26. **All told, the EAP's first criterion was met in terms of Egypt's BOP needs exceeding normal access limits.** The RFI and the SBA were advocated as a means to provide comfort to, and marshal funding from, other financiers so external and fiscal sustainability could be preserved. But they would also serve to shield, at least in part, the banking sector from the impact of a rigid exchange rate regime.

27. **The second criterion for EA has to do with debt sustainability.** It reads: "*A rigorous and systematic analysis indicates that there is a high probability that the member's public debt is sustainable in the medium term. Where the member's debt is assessed to be unsustainable ex ante, exceptional access will only be made available where the financing being provided from sources other than the Fund restores debt sustainability with a high probability. Where the member's debt is considered sustainable but not with a high probability, exceptional access would be justified if financing provided from sources other than the Fund, although it may not restore sustainability with high probability, improves debt sustainability and sufficiently enhances the safeguards for Fund resources.*"

28. **Egypt's debt sustainability analysis raised several warning signs.** The IMF Debt sustainability Framework for Market Access Countries' (MAC DSA) thresholds for the debt burden and for gross financing needs were both exceeded in the baseline scenario (84 percent of GDP versus the benchmark of 70 percent, and 36 percent versus 15 percent, respectively), and more so in the stress tests. The methodology's heat map also yielded warnings: nine out of its 15 cells were red, 3 yellow, 2 "not relevant," and only 1 green. There were also flags in the debt profile: of

[15] The central bank's authorities refer to "Net International Reserves" as their "Tier 1" reserves, while the institution's foreign currency deposits in commercial banks are labelled as "Tier 2."

the five vulnerabilities measured by the MAC DSA in "Higher Scrutiny" cases, only one was considered low risk; the other four were either high or moderate.[16, 17, 18, 19]

29. **While the MAC DSA flagged issues, the staff's assessments for the RFI and the SBA deemed Egypt's debt to be "sustainable but not with high probability" (the so-called "gray zone").** [20] The interviews conducted by the IEO reflect that this assessment was widely considered as sanguine. The judgments involved in the assessment could have been exercised more transparently. The realism check raised a red flag for projected interest rates and staff adjusted the rates up somewhat in the DSA. However, they did not explain the rationale for the judgment nor of its implications for the results. The same adjustment was not incorporated in the program documents, leading to a disconnect between the DSA results and the macro framework. (As noted, the SRDSF has replaced the MAC DSA, improving upon it and incorporating additional tools for judgment (Erce, 2024).)

30. **The assessment was consistent with markets' perceptions.** Had the assessment been "unsustainable," neither the RFI nor the SBA could not have proceeded without first finding enough financing from sources "other than the Fund" to restore sustainability "with high probability." That is, unless other financing materialized, a program would not have been possible without ex ante debt restructuring—a process that can be slow, complex, and costly. This would have also put the IMF in the position of going against the market—five weeks before Board approval, investors had bought US$5 billion in Egyptian Eurobonds—and possibly undermining market access, the very problem the RFI and the SBA were trying to prevent.

31. **As debt was considered to be in the gray zone, emphasis shifted towards mitigating factors and the role of other financing as "safeguards" in the context of EAC2.** Mitigating factors included the high share of local-currency debt held by local institutions (mainly public banks and public insurance companies), the relatively low share of debt held by non-residents, and the government's efforts to extend the average maturity of its Treasury bills. There was also

[16] Egypt's SBA was considered a "Higher Scrutiny" case both because it crossed the thresholds for debt burden and financing needs and because it entailed exceptional access. For reference, see IMF (2013), p.6.

[17] The low-risk cell related to a projected reduction in the share of short-term public debt which, in turn, was an indicative target of the program. Egypt's 2020 SBA debt sustainability analysis was carried out using the MAC DSA methodology. The current Sovereign Risk and Debt Sustainability Framework for Market Access Countries (MAC SRDSF) was approved by the Board in February 2021, the related Staff Guidance Note was issued in August 2022, and its template was uploaded to the IMF website in November 2023 (IMF, 2022b).

[18] The DSA focused on the debt of the "General Government." This is composed of the central and local government, "some" public corporations, the National Investment Bank, and the social security funds. It does not include the spectrum of Economic Authorities and military corporations, which are considered off-budget. The debts of off-budget entities were treated as "contingent liabilities" in the DSA's stress tests.

[19] During the period of the SBA, Egypt's Debt Management Office had not yet developed its capacity to do regular liability management operations, beyond sporadic off-market extensions of maturity for debts held by with state-owned banks.

[20] The High Probability (HP) Tool, an internal tool for staff, was used for making this determination combined with judgment within the IMF's DSA guidelines. The HP tool has since been replaced by the comprehensive SRDSF approved in February 2021, and rolled out IMF (2022b), to succeed the MAC DSA.

fresh access to Eurobonds. All this was thought to provide enough "restructurable" debt in a default event. There were additional financing safeguards. At the time of Board approval, the expected identified financing for fiscal year 2020/2021 was US$9 billion, from Eurobonds, a syndicated loan, and official financing from the World Bank, the Arab Monetary Fund, the African Development Bank, France, and Japan. The World Bank, the second largest official creditor after the IMF, provided budget support after the SBA ended, with a combination of new and restructured investment projects within the existing lending envelope.[21] Its high country exposure and concerns over the macroeconomic framework limited its involvement. In addition, according to several IEO interviewees, the size and speed of Fund financing may have relieved government pressure on other official creditors and had a negative catalytic effect by relieving pressure on official lenders to provide support.

32. **There were no formal guidelines on how much restructurable debt should be considered "enough."** The RFI and SBA DSAs assumed a ratio of three between external public debt (excluding multilaterals) and total Fund credit outstanding expected at the end of the program.[22] This assumption was considered conservative compared to other programs, such as Argentina (2018). But the assumption masked some risks. Its numerator included some US$13.4 billion—about a quarter of all restructurable debt—in foreign official deposits at the central bank that were expected to be extended. The amount was larger than the entire expected financing gap (US$12.2 billion) for that fiscal year—which the IMF and other creditors were to fill. Were those deposits to be withdrawn, the program would not have been viable. Few details were available on the terms, institutional ownership, and decision-making over those deposits. In fact, a few weeks after Board approval, an official deposit of US$2 billion was withdrawn.

33. **The third criterion of the EAP focuses on the prospects for the member to have market access by the time its repurchase obligations to the Fund fall due.** It states that: *The member has prospects of gaining or regaining access to private capital markets within a timeframe and on a scale that would enable the member to meet its obligations falling due to the Fund*. For Egypt, the SBA, together with the RFI and the 2016 EFF, would imply bunched repayments to the Fund in 2023/24 (US$5 billion) and 2024/25 (US$6 billion), equivalent to a quarter of projected central bank reserves. Egypt's future repayment obligations would therefore pose a significant source of BOP needs in particular years.[23, 24]

[21] In normal times, it could be argued that investment lending can be, in effect, budget support if it pays for expenditures that were already in the budget—money is fungible. But, during the COVID-19 outbreak, the spending was almost entirely on items that had not been budgeted for, from personal protective equipment to additional food assistance.

[22] Interviews with IMF staff suggested that, during the internal review process of both the RFI and the SBA, it was decided not to include domestic debt in restructurable debt ratio on two grounds. First, compulsorily reprofiling or restructuring domestic debt would not directly generate additional foreign currency for the government to service its obligations with the Fund. Second, it could lead to domestic financial instability, as Egyptian banks are major buyers of Treasury Bills.

[23] See IMF (2020b), page 12.

[24] "Egypt's GRA credit outstanding after all purchases under the proposed SBA (would) account for over 17 percent of total Fund credit outstanding (second to Argentina, at 38½ percent, by a large margin)." Ibidem.

34. **The positive assessment of the market access criterion was based on Egypt's access to international markets at the time of program approval, confidence in the policy framework, and the authorities' commitment to exchange rate flexibility.** As mentioned, ten days after the approval of the RFI, and five weeks before the SBA was approved, Egypt tapped the international bond market for US$5 billion and was preparing its first green bond (Figure 1). Sovereign spreads, which had peaked at almost 1,000 bps in late March 2020, had fallen back below 600 bps in early June. Prospects for raising further funding during the one-year life of the SBA seemed good. The positive assessment was also supported by an expectation that "close engagement with the Fund" would help the government maintain a "strong policy framework," "reinforce investor confidence," and keep market access open;[25] and the authorities' commitment to exchange rate flexibility—the SBA's Letter of Intent (LOI) stated that, except for "disorderly market conditions," reserves were no longer going to be deployed and would be available to repay the Fund. However, as it turned out, credit ratings did not improve when the news of the RFI-plus-SBA reached the market in late April nor throughout the program.[26]

35. **The final criterion for EA has to do with the prospect for program success.** Specifically, the EAP says: *The policy program provides a reasonably strong prospect of success, including not only the member's adjustment plans but also its institutional and political capacity to deliver that adjustment*. This criterion is relevant in the case of the SBA, as the RFI was not subject to ex post program conditionality, beyond a statement of general policies that the member plans to address its BOP difficulties and not to introduce policies that would compound those difficulties. Egypt's SBA did not entail significant adjustment, given the context of the pandemic. Its performance criteria and indicative targets reflected more accommodative (not tighter) monetary and financial policy. Its structural benchmarks were procedural. That was probably the right approach at the time given the extreme circumstances and uncertainty of the pandemic. Given the short program period and no policy adjustment, prospects for success of the SBA were not hard to establish. Regarding social support, any stigma or political opposition to working with the IMF was overcome by the fact that the country needed help quickly. In addition, the government's track-record of reform built during the 2016 EFF factored in the Fund staff's assessment.

b) Internal Review Process

36. **While the urgency and lack of ex post conditionality of the RFI did not allow for extended technical discussions, the decisions taken on the SBA were subject to internal debate on the risks to the program, including on debt sustainability**. Departmental comments on the Policy Note indicated heightened concerns about risks associated with the

[25] IMF (2020a), Box 3, page 22. However, this kind of assurance seems self-evident, an opposite assessment would mean that the program's design was not up to the task.

[26] A day after the Board approved the RFI, Moody's simply affirmed its B2, five notches below investment grade, and maintained it until it downgraded it in February 2023. A similar pattern by Fitch and Standard & Poor: they had Egypt at B+ and B, respectively, before, during, and after the SBA, only to downgrade it to B and B- in 2023. These were all ratings into the high risk, junk range.

arrangement relative to the note. The conclusion of the public debt sustainability analysis ("sustainable but not with high probability") hinged on a projected decline in the debt burden from 93 percent of GDP at the end of the SBA to 77 percent four years later. That decline, in turn, was predicated on a post-SBA, medium-term fiscal consolidation program, the details of which were unknown. More specific measures and assessment of risks might have been useful. Staff proceeded based on the authorities' commitment—expressed in the LOI—to reach and maintain a primary surplus of at least 2 percent of GDP as soon as the pandemic ended. Other fiscal benchmarks were also general and procedural: the cabinet approval of a medium-term revenue strategy, the completion of a Public Expenditure Review with World Bank support, and the update of the medium-term debt strategy.

37. **There were discussions about the risks associated with a worse than expected COVID-19 outbreak, the reliance on exchange rate flexibility, and the systemic impact of the NIB.** On COVID-19, a contingency plan for a downside scenario was proposed. Staff would deliver one, which was discussed with the government but not in the published reports. The plan assumed a second wave of COVID-19 over 2021 and entailed major policy challenges and efforts. During internal discussions, doubts remained on whether the exchange rate flexibility would come to pass—as explained before, it did not. It was seen as critical to avoid an excessive accumulation of non-resident holdings of public domestic debt (that is, volatile carry trade), cushion the macroeconomic framework should the pandemic worsen, and safeguard the Fund's financial position (the assessment of reserve adequacy metrics was based on a floating foreign-exchange regime). There were calls for two-sided flexibility to be part of the conditionality. That did not happen. Instead, the matter was confined to the LOI. There were also discussions about the systemic risk posed by the NIB as an institution that held deposits from the public but was outside the central bank's supervisory perimeter. The program included a structural benchmark on the development of a reform plan of the NIB, much of which had been considered in the 2016 EFF, but no further conditionality on the NIB.

38. **Some relevant risks were not raised during the staff-level review, according to the documentation.** For example, the impact of the pandemic on the soundness of the banking system was not assessed—and in fact would have been hard to assess given that the data then available ended in 2019. Neither was the steep fall in the net foreign assets of the banking system, caused by the central bank withdrawing its foreign currency deposits to replenish its official "Net International Reserves." Also not assessed was the apparent practice of asking state-controlled banks to contribute to stabilizing the exchange rate by selling foreign currency into the market at the expense of their own capital positions. There was no deep enquiry about the assurances that the deposits that Gulf Cooperation Countries (GCC) held at the central bank would be rolled over. And the origin, drivers, and volatile nature of the large portfolio flows that seemed to be conditioning the exchange-rate policy stance were not analyzed. Additionally, the governance of crisis-related spending was only marginally developed. While the RFI required a policy for tracking, reporting, and auditing of outlays and of awarded contracts to ensure that Fund resources were used for pandemic-related purposes, no policy to that end was included in

the program's criteria and commitments were only made in the LOI. Some of those commitments were met—like the publication of procurement contracts—and some were not—like disclosing the status of execution of non-health, crisis-related expenditures.

39. **Overall, however, the internal discussions conveyed a sense that the SBA carried much unhedged risk**. There were many unknowns and a heavy reliance on policy commitments in the LOI rather than on conditionality. There was genuine uncertainty about the pandemic, especially if the health emergency were to last more than one year. The SBA's design did not effectively mitigate the risks raised during its internal review, with conditions being watered down or removed between the Policy Note and the staff report for the program request. The emergency and urgency of the moment may have been strategic reasons at the institutional level to call on the EAP and go ahead, given the enormous risks associated with the Fund not providing needed support.

40. **The internal discussion did not envisage the better-than-expected outcome that materialized.** There were no requests for a built-in mechanism to capture upside risk—say, by adjusting up central-bank reserve accumulation, or trimming down the size of the SBA purchases, or starting earlier the fiscal retrenchment if the crisis turned out to be short-lived. Whether such a mechanism was possible in a 12-month-long program with only two reviews is an open question. But at least some discussion would have been useful.

c) Following an Enhanced Decision-Making Process

41. **Beyond technical criteria, the EAP requires a "higher burden of proof" in program justification and early consultations with the Board (Box 1)**.[27] How were those two requirements followed in Egypt's 2020 RFI and SBA, given that the country was struck by a once-in-a-century shock over which it had no control and fast action was called for?

42. **Within their working assumptions, IMF staff delivered a consistent rationale for both the RFI and the SBA.** Compared to the package for Board approval of the 2016 EFF—which was a "normal access" arrangement—the 2020 RFI and the SBA included four pieces of extra analysis as mandated by the EAP. They were assessments of the sources and uses behind Egypt's financing gap, of how EAP criteria were met, of the impact that EA would have on the Fund's finances, and of the country's capacity to pay back the Fund.[28] Taken together, they argued in favor of proceeding, while acknowledging the risks associated with a bunching of repayments to the IMF and with implementation of key policy commitments, including exchange rate flexibility.[29]

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[27] See IMF (2003).

[28] The latter two assessments were jointly produced by the Finance Department and the Strategy, Policy, and Review Department (IMF, 2020b).

[29] The assessments were not all produced by the same departments within the Fund, but their texts overlap considerably—for instance, in describing the mitigating factors around risks.

Box 1. Informal Board Consultation Procedures for EAP

1. Once Management decides that exceptional access may be appropriate, it will consult with Board promptly in an informal meeting that will provide the basis for consultation with capitals and help identify issues that would be addressed in a further informal session.
2. Directors are to be provided a concise note circulate at least two hours before the informal meeting that includes as fully as possible: (i) a tentative diagnosis of the problem; (ii) the outline of the needed policy measures: (iii) the basis for judgment that exceptional access may be necessary with a preliminary evaluation of the four substantive criteria, and including a preliminary analysis of external and sovereign debt sustainability; and the likely timetable for discussions.
3. Before the Board's formal consideration of the UFR staff report additional consultations will normally be expected to keep the Board abreast of program-financing parameters including: (a) assumed rollover rates; (b) economic developments; (c) progress in negotiations; (d) any substantial changes in understandings; and any changes to the initially envisaged timetable for Board consultation.
4. In this connection, staff will provide the Board with a separate report evaluating the case for exceptional access based on further consideration of the four substantive criteria, including debt sustainability. Where time permits, this report will be provided to the Board in advance of the circulation of program documents. In all cases, this report will be included with the program documents.
5. Management will consult with the Board specifically before concluding discussions on a program and before any public statement on a proposed level of access.
6. Strict confidentiality will need to be maintained and public statements by members, staff, and management should take special care not to prejudge the Board's exercise of its responsibility to take the final decision.

Sources: IMF (2003; 2004).

43. **The EAP also calls for early consultations with the Board at three stages in the decision-making process:** once management establishes that EA may be appropriate but before negotiations with the authorities start; after a first round of negotiations but before staff-level agreement is reached; and, before the formal Board presentation. The first one is required while the others are normally expected. In Egypt's case, and in a reflection of how urgency may have prevailed over EAP guidance, only one consultation took place for each the RFI and the SBA, on April 27 and May 22, 2020, respectively. Both consultations were based on concise notes—"Staff Statement"—which cast, in a synthetized way, the financing gaps, objectives, tools, policies, and risks that would subsequently appear in the documents for Board approval. The notes also included tentative levels of access of, respectively, US$2.8 billion and US$5.2 billion—the eventual actual amounts—and preliminary assessments of EA criteria. They did not analyze the risk and impacts of either operation on the Fund's finances—likely due to lack of time. In terms of the staff's strategy and plans, the consultations led to no changes in direction.[30]

44. **At the approval stage, the Executive Board's formal deliberations mirrored the internal review by staff.** The Board unanimously approved the SBA while reflecting on vulnerabilities and risks of the program. Executive Directors were keen to support a member dealing with a global emergency and, along the way, find a replicable model for other members who may

[30] In what was possibly a logistical slippage during the turmoil of the pandemic, the government publicly announced its request for the RFI and the SBA on April 26, 2020—that is, one day before the single consultation with the Board on the RFI took place, and well before any consultation for the SBA.

request similar support. But two themes recurred in the discussion: the relatively limited structural conditionality—leaving vital reforms to the LOI—and the criticality of the foreign exchange regime—any rigidity would make the recovery harder and lessen the safeguards for the IMF. Suggestions were made to recalibrate the program as soon as the worst of the pandemic was over.

d) Ex Post Evaluation

45. **The EAP requires that Fund staff conduct an evaluation of EA programs within one year from the end of the arrangement.** The policy is not applicable to RFIs. That is why in Egypt's case only the SBA was evaluated; this EPE was completed in June 2022 and discussed by the Board a month later.[31, 32] The findings speak of success in achieving the operation's main objective—to preserve macroeconomic stability in the face of the pandemic. They acknowledge that demands for adjustment were non-existent: fiscal, monetary, and financial policies were eased to accommodate extra social spending and economic stimuli.[33] They argue that momentum was "kept on structural reforms in selected areas." All program conditionality were met and reviews were completed on time.

46. **That positive conclusion is confounded by an unexpected development: the impact of COVID-19 on the economy was major, but much less and much shorter than originally envisaged.** Both external and domestic confidence returned halfway into the program. So did portfolio inflows. The baseline scenario of continuing deterioration, while sensible at entry, proved too pessimistic. This makes attribution difficult: was the return of private financiers due to the SBA—and, more generally, the support of the IMF—or to surprisingly better global conditions? Were portfolio flows attracted by the economy's resilience and improving long-term outlook, or by three-month Egyptian Treasury bill rates hovering around 15 percentage points per annum above U.S. Treasuries, with a nominal exchange rate that was kept upward rigid? Like the government, the EPE saw the quick return of portfolio capital as a sign of program success. The authorities took it as a sign of renewed confidence in Egypt, and the Fund as a safeguard for Fund resources, despite the risks associated with carry-trade. It was based on a combination of interest rate differentials and an inflexible foreign exchange system.

47. **The EPE focuses more on describing outcomes than questioning impacts—the "whats" more than the "whys."** It highlights four lessons. First, the government's commitment to two-sided exchange rate flexibility was not met.[34] This fostered a worrisome reliance on

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[31] IMF (2022a), page 1.

[32] The EPE (IMF, 2022a) notes that EPEs are not applicable to outright purchases under the RFI that involved exceptional access, in line with the EPE Guidance Note (IMF, 2010).

[33] The EPE (IMF, 2022a) describes well the spirit of Egypt's SBA: "The general policy direction given to the membership was to 'spend as much as you can, but keep the receipts'." Idem, Box 1, page 10.

[34] The EPE does not explore why the authorities declined to float the exchange rate. Interviews with officials and with stakeholders pointed to several, not-equally-valid concerns: (i) the social impact of a pass-through to inflation; (ii) lack of export response by a private sector that is constrained by broader regulatory impediments; (iii) a political perception that a "strong country needs a strong currency;" (iv) the commercial banks' negative net foreign asset positions; (v) triggering a sudden capital flight by foreign portfolio investors ("carry-traders"); and (vi) it is "an IMF issue."

short-term capital inflows—and an exposure to their sudden reversal. Second, the definition of Net International Reserves of the central bank ignored its foreign-currency deposits in local banks, which posed a risk to the banking system. Third, the SBA did not include a mechanism to capture upside risk: how to adjust the program's targets or its purchases if things turned out better than expected? And fourth, there was relatively little analysis and discussion of the deposits of GCC countries at the central bank although they were a key source of financing.

48. **The EPE is correct in its claim that the principal objective of the SBA was achieved.** That is, the stability of the economy was preserved in the face of the massive fiscal and BOP shocks that the pandemic had caused. This was to happen through an injection of liquidity via the RFI and the SBA, which would keep funding from creditors and donors coming. Whether that liquidity made all the difference is debatable as it was dwarfed by an unexpected return of portfolio flows. Structural policies, on the other hand, were given relatively less priority. Structural benchmarks, which were procedural, were easily met. But actual reforms were deferred. That begs the question: What makes an IMF program successful? The EPE chose to consider success in terms of the program meeting its objectives and conditionalities enough rather than also to take into account the before and after vulnerabilities of the economy.

49. **A notable aspect of the EPE was its relative silence about the unmitigated risks embedded in the SBA.** As mentioned, conditionality did not cover some key policies—such as exchange rate flexibility and post-crisis fiscal adjustment;[35] there was no feasible contingency plan, had the pandemic lasted another year; the systemic risk of the NIB was not considered; and there was not enough exploration of the risks of wide fluctuations in portfolio flows despite Egypt's non-investment-grade, sovereign credit rating and reliance on GCC deposits (which can be driven by non-economic considerations). The EPE did not elaborate on why the SBA did not mitigate these risks to the program. One explanation is the program's duration—there is so much a government can implement in 12 months, especially when its hands are full dealing with a pandemic. A short horizon also blunts the idea of a mechanism to capture upside risk: by the time the first review gathers the new data, there is only one review left to implement any correction. However, a longer program could have been an option.[36] Another explanation is that IMF staff had been advised by their Board and management to favor "streamlining conditions to maintain parsimony,"[37] which generally implies keeping conditions to a minimum and trusting

[35] A case can be made that, in Egypt, the *quality* of fiscal retrenchment—and, more generally, fiscal consolidation—is as important as its *quantity*. The part of the economy actually subject to taxation is very small, as many productive sectors are either under military control or in informality. With rigid expenditures, past fiscal adjustments have tended to translate into heavier tax burdens on a relatively few, private formal businesses. This was an issue the SBA did not focus on.

[36] Only three months after Egypt's SBA went to the Board, Ecuador received a 27-month, US$6.5 billion EFF; both operations triggered the EAP, both were preceded by RFIs, and both were focused on protecting macroeconomic stability from COVID-19.

[37] IMF (2019b).

the rest to the LOI.[38] Whichever the reason, this left serious exposures open. By elaborating on them, the EPE could have distilled valuable lessons for future EAP-backed engagements.

50. **Lastly, there is not much reference in the EPE to the commitments made in the LOI.** Some commitments were met, others were not such as exchange rate flexibility and fiscal retrenchment, as mentioned, as well as those related to tax collection, the business environment, the role of state-owned enterprises, trade facilitation, and the NIB. The EPE does not analyse why implementation fell short of commitments in these areas. Long-standing, political economy constraints may have played a role. This is an area into which the SBA preparations did not delve, because of lack of time, expertise, or both. Such analysis may have led to a more nuanced formulation of policy objectives and actions (such as to consider bringing some state enterprises under the same legal and tax frameworks as the private sector, rather than seeking their outright privatization).

IV. EVALUATION OF OUTCOMES: DID THE EAP-ENABLED RFI-SBA COMBINATION WORK?

51. **It has been more than three years since the Egypt's SBA concluded.** New information about the country's economy and policies has become available. A new IMF EFF program has been approved and is on-going. This provides a rich basis to assess whether invoking the EAP back in 2020 to deliver the RFI and the SBA worked. It also raises the duty of all evaluations: to separate the quality of the initial decision from the quality of the outcome.

52. **Under the circumstances of mid-2020, calling on the EAP to put forward a rapid package of support for Egypt seems the right institutional call.**[39] A member country was being battered by a global emergency and was given immediate financial support. But it was also a call loaded with risk—much of which went unhedged. There was no binding conditionality to correct important vulnerabilities and policy mis-alignments—among others, in fiscal consolidation, debt sustainability, and exchange rate regime. And had the pandemic lasted beyond 2021, formidable policy efforts would have been necessary.

53. **The COVID-19 crisis had less economic impact and subsided much faster than expected in the program, whose expectations—in hindsight—proved pessimistic.** The judgement in June 2020—when the arrangement went to the Board—was that exceptional funding was necessary because the worst impact of the crisis was to come in fiscal year 2020/2021.[40] That did not happen. While the projected drop in tourism did arrive, Suez Canal receipts and remittances not only did not fall but rose—the latter to record levels. Below the line, while FDI stayed relatively low, portfolio *inflows* were five times larger than before the pandemic.

[38] There seems to be little evidence that less reforms lead to better reforms. Parsimony and macrocriticality have not provided incentives for IMF program teams to increase the quality of structural conditions. See Kim and Lee (2021).

[39] As explained before, because of the pattern of previous access, a package of virtually any size necessitated triggering the EAP.

[40] Both the pessimism and the view that the pandemic would last one year were found in other crisis-response programs of that time (IEO, 2023a).

The dreaded capital flight that had hit Egypt in the second quarter of 2020 was more than reversed. The government even managed to tap the international capital market for a total of almost US$10 billion—including an oversubscribed US$750 million green bond.

54. **Rather than facing upward pressure, the nominal exchange rate appreciated slightly and returned to pre-crisis levels.** With no need to defend that rate, the worrisome withdrawal of foreign-currency deposits by the central bank from commercial banks stopped. Reserve accumulation by the end of the program was twice what the performance criteria required (US$6.3 billion, instead of US$3.3billion). Core macroeconomic variables followed suit: growth, initially projected at 2 percent per annum over fiscal year 2020/21, turned out to be 3.4 percent, and inflation topped at 4.5 percent instead of the expected 9 percent per annum.

55. **The realization that the baseline scenario was too grim came early in the program.** In fact, it was becoming evident during the First Review in December 2020 and was solidified during the Second in June 2021 (see Table 2). The former's document summed up the situation in its very first sentence: *The disruption to economic activity in the June quarter was less than expected.*[41] From start to end, the quantitative performance criteria on reserve accumulation and primary surplus were overperformed. Inflation was so much less than initially projected that the *lower* outer band of the program's Monetary Policy Consultation Clause was breached.

56. **In other words, the Egyptian economy weathered the COVID-19 emergency remarkably well.** The RFI and the SBA and their use of the EAP certainly contributed to that—even though causative attribution is difficult. Having large, rapid, and public support—technical and financial—from the Fund must have been reassuring for markets. Interviews with both domestic and foreign investors with financial positions in Egypt confirmed that impression. They also confirmed that the markets' positive sentiment about Fund support outweighed concerns among private creditors about the subordination of their claims.

57. **But success at short-term stabilization may have come at the price of postponing and, perhaps, entrenching structural vulnerabilities.** Four of them need mentioning. First, exchange rate rigidity, with the concomitant loss of a natural buffer against further external shocks, was never abandoned. Second, partly because of that rigidity, during and immediately after the SBA, there was a ballooning of non-resident holding of Treasury bills. With uncovered interest rate differentials in double digits and a perceived policy attachment to nominal exchange rate stability, "hot money" inflows burgeoned. While the Second Review of the SBA spoke of "the

[41] IMF (2020c).

authorities' continued commitment" to two-side exchange rate flexibility, markets were betting that upward pressure on the rate would not be allowed.[42, 43]

Table 2. By December 2020, The Baseline Scenario Had Proven Over-Pessimistic
(In billions of U.S. dollars)

	2018/2019 Actual	2019/2020 Estimated at the time of SBA's Board Approval	2020/2021 Projected at the time of SBA's Board Approval	2020/2021 Projected at the time of First Review	2020/2021 Projected at the time of Second Review
Tourism	12.6	10.0	2.7	2.4	4.4
Suez Canal	5.7	5.2	4.9	5.7	5.9
Remittances	24.8	21.6	18.7	24.2	29.2
Current Account Balance	-10.9	-14.8	-16.2	-16.5	-15.4
FDI (net)	7.9	8.0	5.5	5.4	5.4
Portfolio Flows	4.1	-7.5	3.5	9.6	20.2
NFA of Local Commercial Banks	2.2	-4.0	-6.2	-1.7	-2.0
External Financing Gap	0.0	-9.2	-12.2	-12.2	-10.9

Source: IMF – Arab Republic of Egypt: Staff Report for the 2021 Article IV Consultation and Second Review under the Stand-By Arrangement, June 7, 2021.

58. **Third, retrenchment from the temporarily-loose fiscal stance that the SBA had supported never happened**. If anything, the primary balance stayed at pandemic levels. One year after the arrangement concluded, a third of public expenditures was accounted for by interest payments, which were equivalent to about half of fiscal revenue. The medium-term revenue strategy was not implemented and tax collection remained stubbornly low at around 12 percent of GDP. The medium-term decline in the sovereign debt burden, from 93 percent of GDP to 77 percent in fiscal year 2024/2025 was no longer reachable. Neither was debt sustainability "with high probability."

59. **And fourth, while the structural agenda of the SBA only sought to keep "momentum" through procedural steps, reforms that would rein on off-budget entities and expand the economic space for the private sector or boost its competitiveness did not materialize.** Neither actual trade facilitation—internal or domestic—nor privatizations of state-owned enterprises took place. The SBA was not only light on reform but many of the reforms it did carry failed during implementation. Take the new Customs Law expected under the program: in practice, it does not apply to off-budget entities. Or take the amendments to the Competition Law: they gave no voice to the Egyptian Competition Authority to opine on preferential treatments for those entities. A similar pattern applies to the new Banking Law ratified in September 2020. While this law gives more independence to the central bank, it also calls for its permission to sue commercial banks; this, in practice, grants legal immunity to state-controlled banks. This raises questions about not just the authorities' capacity to implement reforms, but

[42] By then, Fund staff had to reclassify Egypt's foreign exchange regime from "de-jure floating" to "de facto stabilized." See IMF (2021).

[43] Interviewees expressed mixed opinions on exchange rate flexibility. Many non-IMF stakeholders pointed to the limited impact on exports of past devaluations, owing to supply side structural impediments to private sector activity, while pointing to the high social cost from pass-through to inflation.

also about the Fund's capacity to follow up on structural reforms and monitor them over time, by itself or by partnering with specialized multilaterals.[44]

60. **In brief, the IMF leaned forward, deployed its EAP, and took on significant risks to help Egypt financially and technically at a moment of urgency and uncertainty.** Helped in addition by positive surprises, the economy avoided the worst of the pandemic. But, in retrospect, the crisis and the exceptional support it elicited missed an opportunity to tackle reforms that had proven so elusive during normal times. The country—and its obligations to the Fund—remained widely exposed to external shocks.

61. **Two such shocks came soon and in quick succession.** In late February 2022, Russia invaded Ukraine, causing a spike in the price of fuel and food—dominant imports in Egypt's balance of payments. Just a month later, the US Federal Reserve started its process of quantitative tightening and, with it, of raising its policy rate—which would eventually rise from almost zero to more than 5 percent in less than two years. More expensive imports and tightening international financial conditions followed. Confidence on the Egyptian pound began to ebb. The US$18 billion portfolio *inflow* of fiscal year 2020/21 became a US$21 billion *outflow* in 2021/22. The central bank lost US$11 billion of its foreign-currency reserves. A new external financing gap—worth about US$6 billion—began to develop. The stability gains of the SBA were gone.

V. CONCLUSIONS: WHAT CAN WE LEARN FROM DEPLOYING THE EAP IN EGYPT'S 2020 RFI-SBA?

62. **The pandemic had a vast and immediate human and economic toll on Egypt.** The 2020 exceptional access under the RFI and the SBA provided timely support, helped stem the panic, and encouraged a return of capital inflows. However, partly reflecting its short duration, the arrangement did not address key vulnerabilities and was seen by many as a "a missed opportunity" to set Egypt on a stronger path to medium-term viability.

63. **What can be learned from this process and, more relevant, from its use of the EAP? Several lessons can be drawn. First, the EAP, and perhaps the Fund's lending framework more broadly, could *systematically* incorporate a mechanism to capture upside risk that leads to lower-than-projected BOP needs.** By its first Review, it was apparent that the SBA was built on too pessimistic a scenario. Adjustments to policies were warranted—for example, rolling back part of the loosening of the fiscal stance. New or deeper reforms could have progressed beyond preparatory steps, notably in shifting the boundaries between private and public sector. But to make those changes, a program horizon of only 12-months seems short—by the time a review could detect the problems, there would be no or only one review left to address them.

[44] The gap between intentions and outcomes was not unique to the 2020 SBA and may be perennial in Egypt. Under the 2016 EFF a new Public Procurement Law was passed in October 2018: it included a single article that invalidated its effect over many, if not most, government purchases (the article exempts Economic Authorities from the law when they buy from military companies).

64. **Second, political-economy analysis could usefully complement the risk assessments in EA requests**. Horizons longer than just one year for Fund-supported programs involving EA could give governments more time to implement corrections.[45] Both steps would be useful in managing the broader enterprise risks for the Fund. Also, structural reforms that are pivotal for lasting macroeconomic stability need to be properly designed, implemented, and followed-up—by the IMF itself or by partnering with an expert institution.

65. **Third, the EAP's second criteria can be hard to assess and apply, requiring difficult judgments from IMF staff.** When a member has recently tapped the market and is current on its obligations, can its public debt really be judged as "unsustainable" and a program be conditioned on prior debt restructuring? In principle, yes—but in practice it can be difficult. In Egypt, the implications of declaring debt unsustainable could have been extremely costly for both the country and the IMF: a member in good standing and with market access struck by a one-in-a-century crisis not of its making comes to the Fund for help and walks away with a financial meltdown. Instead, the Fund used judgment. The result was MAC-DSA and HP Tool thresholds that flashed red and a staff assessment that did not.

66. **Fourth, assessments of future prospects for market access would benefit from more consistent methodology.** Such assessments can be difficult for countries with volatile capital flows. Otherwise, teams may have little to go on besides historical market access, which is however an unreliable guide to future market access.

67. **Fifth, the EPE described outcomes (what happened) but did not explain the reasons behind those outcomes (why they happened)**. Such analysis would have provided a much richer source of learning. So would have consultations with a broader and more diverse set of external stakeholders.

68. **Finally, when the EAP is used during a crisis or emergency, there may be little time to meet the EAP's procedural mandates.** These include the additional analysis (an "enhanced burden of proof"), the suggested doubled-up decision-making, and additional consultations with stakeholders.

[45] A similar recommendation for programs in the Middle East and Central Asia was made in Mecagni and Kincaid (2021).

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