Independent Evaluation Office
of the International Monetary Fund

DRAFT ISSUES PAPER

IMF ENGAGEMENT IN SMALL STATES

JUNE 24, 2020

I. INTRODUCTION

1. This issues paper lays out the motivation, themes, and scope for an IEO evaluation of the IMF's engagement in Small Developing States (SDS).[1] It will be discussed with the Executive Board and IMF staff and posted on the IEO website to elicit comments.

2. The IMF's engagement with its smallest members faces a number of specific challenges. As members, these countries are fully entitled to access Fund financial and capacity development resources and policy advice, while their lack of scale, often remote location, and vulnerability to natural disasters lead to particular needs. The devastating impact of the current COVID-19 pandemic on SDS illustrates how vulnerable these countries are to exogenous shocks, both directly and through second round effects. Moreover, notwithstanding their tiny overall weight in the global economy, SDS play a significant part in international financial flows, with more than half of these countries being considered offshore financial centers by the IMF.[2] Against this background, concerns have been raised whether the Fund could do more to help SDS achieve their macroeconomic goals within its limited overall resource envelope, with particular concerns expressed about the high turnover of staff working on these countries.

3. While several recent IEO evaluations have touched on issues relevant to SDS,[3] the new evaluation will focus specifically on the IMF's engagement with this group of countries for the first time. Findings and recommendations may also be relevant to the Fund's work on a wider segment of the membership that may also be increasingly subject to climate change, natural disasters, and health-related emergencies. There may also be useful general lessons from SDS experience related to mission turnover, cross-country knowledge-sharing, and the integration of surveillance and capacity development.

II. BACKGROUND

4. The IMF classifies as SDS those members with populations under 1.5 million, excluding advanced economies and fuel exporting countries (as defined by the WEO). A total of 34 countries, or 18 percent of the IMF's membership, fall into this category (Table 1). Among this group, 27 are island states, 5 are coastal, and 2 are landlocked; 12 are in the Caribbean, 11 in the Pacific, 7 in Africa, and 4 in in Europe and Asia. Fifteen of them are "microstates," with populations below 200,000, 6 of them have populations under 100,000 and the smallest has a population of 10,000. Eight are considered to be in a fragile or conflict-affected situation (FCS). In terms of income level,

[1] The IMF uses interchangeably the terms "small states" and "small developing states." The evaluation will also follow this practice.

[2] The IMF defines an offshore financial center as a country or jurisdiction that provides financial services to non-residents on a scale that is incommensurate with the size and the financing of the its domestic economy.

[3] Relevant ongoing and prior reports include: Working with Partners: IMF Collaboration with the World Bank on Macro-Structural Issues (IEO, 2020; forthcoming); Adjustment and Growth in IMF-Supported Programs (IEO, 2021; forthcoming); *The IMF and Fragile States* (2018); and *The IMF and Social Protection* (2017). About one-third of SDS have featured as country case studies in previous IEO evaluations.

11 are considered lower-middle, 16 are upper-middle, and 7 are high-income countries, using World Bank criteria.[4] The 34 SDS represent 0.13 percent of global GDP and 0.2 percent of global trade and global population. The World Bank uses an expanded list of 50 countries, including all IMF-defined SDS, together with 3 fuel exporting countries, 5 advanced countries, as well as 8 countries with populations greater than 1.5 million but sharing many of the characteristics of SDS. Collectively these 50 countries are members of the Small States Forum (SSF).[5]

Table 1. Small States as Classified by the IMF and World Bank

		AFR	APD	EUR	MCD	WHD
WB (50)	**IMF (34)**	Cabo Verde Comoros Eswatini Mauritius Sao Tome & Principe *Seychelles*	Bhutan Fiji *Kiribati* Maldives *Marshall Islands* *Micronesia* *Palau* *Samoa* Solomon Islands Timor-Leste *Tonga* *Tuvalu* Vanuatu *Nauru*	Montenegro	Djibouti	*Antigua & Barbuda* Bahamas Barbados Belize *Dominica* *Grenada* Guyana *St Kitts & Nevis* *St Lucia* *St Vincent & the Grenadines* Suriname Trinidad & Tobago
		Botswana (>1.5m) Eq. Guinea fuel exp.) Gabon (>1.5m) Gambia (>1.5m) Guinea Bissau (>1.5m) Lesotho (>1.5m) Namibia (>1.5m)	Brunei (fuel exp.)	Cyprus (adv.) Estonia (adv.) Iceland (adv.) Malta (adv.) *San Marino (adv.)*	Bahrain (fuel exp.) Qatar (>1.5m)	Jamaica (>1.5m)

Source: IMF and World Bank.
Note: Microstates are shown in italics. AFR=African Department, APD=Asia and Pacific Department, EUR=European Department, MCD=Middle East and Central Asia Department, WHD=Western Hemisphere Department.

5. SDS comprise a heterogeneous group but share many similar characteristics and vulnerabilities which pose particular challenges for development and macroeconomic stability. Due to their small population and economic size, they have narrow production and export bases and experience serious constraints on institutional and human resource capacity, which limit governments' ability to provide public services, a particularly acute challenge for microstates. Relatedly, a number of social issues such as youth unemployment and outward migration from the highly educated pose substantial concerns for SDS. Many SDS also suffer from remoteness and insularity, raising trade transportation costs. In addition, their narrow economic bases mean that they are relatively open, making them more susceptible to macroeconomic volatility,

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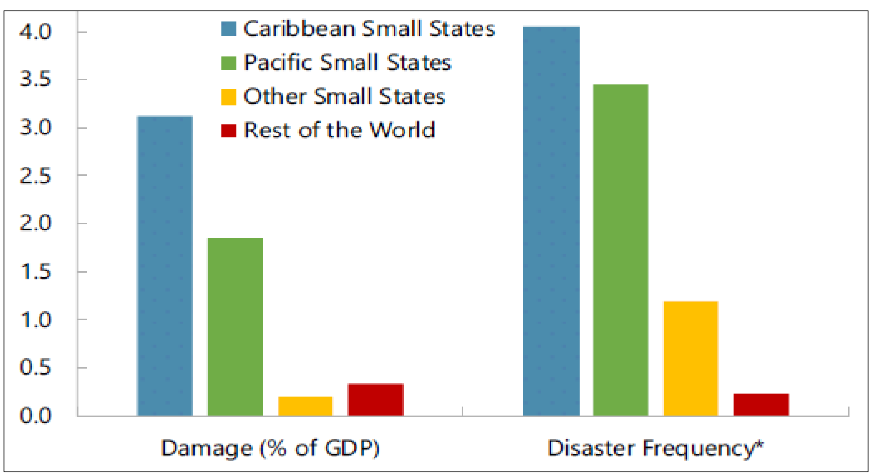
[4] The World Bank classifies countries by income per capita. For 2020, countries are classified as follows: low-income countries (per capita income of $1,025 or less), lower-middle-income countries ($1,026-$3,995), upper-middle-income countries ($3,996-$12,375) and high-income countries ($12,376 or more).

[5] The SSF is a high-level platform for international dialogue on small states issues, hosted by the World Bank.

commodity price fluctuations and disruptions in world markets, and highly exposed to terms-of-trade shocks and volatile trade tax revenues. Domestic financial systems in SDS are typically shallow and regulatory and supervisory institutions are often weak. At the same time, many SDS operate offshore financial centers, which can face particular challenges in complying with international standards, including in anti-money laundering and combating the financing of terrorism (AML/CFT).

6. Crucially, SDS are among the most vulnerable countries to climate change and natural disasters. Eighteen out of the 20 most exposed countries in the world are on the Fund´s list of SDS.[6] Especially in the Caribbean and Pacific regions, they suffer much greater economic consequences from natural disasters, and more frequently, than other economies (Figure 1). Many SDS are located in regions prone to hurricanes, cyclones, and tsunamis and those in the Pacific region are also highly vulnerable to sea-level rise. These factors have macro-critical effects, including immediate economic disruption from disasters, sizeable contractions in output and exports, disaster-related expenditures for social needs and rebuilding, abrupt declines in fiscal revenues, and increased imports. At the same time, increased vulnerability translates into a need for ample buffers to provide resilience against disaster risks, including adequate official reserves, low debt levels, strong fiscal and external positions, effective insurance mechanisms, and reliable access to financing.

Figure 1. Effects of Natural Disasters, 1980–2017
(Annual average)



Source: IMF (2019a).
***Note:** Frequency is the annual average of all natural disaster incidents from 1980–2017 per 10,000 sq. km. of land area.

7. The ongoing COVID-19 pandemic is imposing a heavy toll on most small states. Many are largely tourism-dependent and have seen this sector come to a sustained halt since mid-March 2020, with ripple effects across their economies. The rapid curtailment of commercial activity and additional direct health and social expenditures have boosted fiscal deficits and

[6] Based on the UN's 2018 Exposure Index.

balance of payments pressures. Governments have swiftly implemented containment measures that have been quite successful in flattening the curve of the spread of the virus and taken action to help mitigate the economic and social impact of the pandemic, with scarce budgetary resources reallocated to critical health care spending and income support. In some cases, the effects of the COVID-19 outbreak has been compounded by other disasters, including in Samoa, which suffered from a severe measles outbreak in late 2019; and Fiji, Solomon Islands, and Vanuatu battered by Cyclone Harold in April 2020.

8. Within the group of SDS, those in the Pacific and in the Caribbean display distinct regional characteristics (IMF 2017). SDS in the Pacific region (which include the largest number of microstates) are poorer, more dependent on official development assistance, more remote, and more widely dispersed than small states in other regions. Their economies are also smaller, with the GDP of all Pacific SDS representing approximately a fifth of the combined GDP of Caribbean SDS. By contrast, most Caribbean SDS are larger and qualify as upper middle-income countries. However, their public debt as a share of GDP (80 percent in 2016) is substantially higher than in Pacific SDS (32 percent in 2016), and many have run into serious debt related stress and needed debt restructuring.

9. The vulnerabilities described above make SDS particularly dependent on support from external partners and the international community for policy analysis, advocacy, risk pooling, access to finance, and technical expertise. Consequently, various regional, multilateral and other partnerships and structures for collaboration with and support for small states have developed over time.[7] These include multiple regional institutions, including the Eastern Caribbean Central Bank (ECCB), the Caribbean Community and Common Market (CARICOM), the Organization of Eastern Caribbean States (OECS), and the Pacific Islands Forum Secretariat (PIFS), the Pacific Regional Environment Programme (SPREP), and the Melanesian Spearhead Group (MSG). Multilateral institutions with strong engagement include the World Bank and the United Nations (UN).[8] At the plurilateral level, the Commonwealth has provided analytical and policy support on SDS' vulnerabilities and lack of resilience and global advocacy for its 32 small states members (23 of which are in the IMF's list of SDS) since the 1960s and the Alliance of Small Island States (AOSIS) promotes the interests of SDS in global economic, trade and other fora. Regional risk pooling arrangements have been established to pool climate and natural disaster risks in SDS in the Caribbean and the Pacific regions.[9] In addition, there are long-standing bilateral partnerships for technical assistance between, for example, Australia and New Zealand with Pacific SDS and Canada with Caribbean SDS.

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[7] While the potential gains from regional collaboration are significant, SDS are also competitors in some respects (e.g., the tourism sector).

[8] For example, the World Bank supports the annual SSF, provides extensive policy support, and provides concessional lending to SDS through its IDA window; the United Nations provides support to Small Island Developing States through the UN's Office of the High Representative for Least Developed Countries, Land-Locked Developing Countries and Small Island Developing States (UN-OHRLLS).

[9] For example, the Caribbean Catastrophe Risk Insurance Facility (CCRIF).

III. IMF ENGAGEMENT WITH SMALL STATES

Legal mandate and governance

10. As IMF members, SDS receive policy advice through regular IMF surveillance under Article IV; have access to support from the Fund through a range of lending facilities and non-financial instruments; and benefit from the Fund's provision of capacity development.[10] There is no specific mention of SDS in the Articles of Agreement, in the conditionality guidelines, or the integrated surveillance decision, and there is no Board-approved list of SDS. The IMF's SDS classification is intended to define an operational group of member countries with particular needs, providing for targeted analysis to determine how the Fund can best meet those needs.[11] Analytical surveillance tools relevant for SDS are described in the Background Studies of the Triennial Surveillance Review and Executive Board engagement on SDS' resilience to natural disasters and climate change is covered in the 2018 Interim Surveillance Review. In addition, SDS qualify for less restrictive eligibility and graduation criteria for Poverty Reduction and Growth Trust (PRGT) resources, although their income per capita is above the usual IDA cutoff.[12]

11. While the 34 SDS represent 18 percent of the IMF's membership, they make up a much smaller fraction of the Fund based on other metrics (see Table 2). Their total quota share is 0.39 percent (using the World Bank classification, their combined quota rises to 1.19 percent). They have 1.31 percent of the voting share, which includes 0.92 percent of basic voting shares as well as 0.39 percent of quota-based shares. At the Executive Board, SDS members are distributed across 9 constituencies, although most are concentrated in four constituencies. In early 2012, the IMF's Executive Board established an informal working group on SDS, made up, inter alia, of a core group of Directors representing SDS in the Caribbean, Pacific and Sub-Saharan Africa.

Table 2. Small States Footprint
(In percent of global aggregate)

GDP	Population	Trade	IMF Membership	IMF Quota	IMF Voting Share	IMF Spending on Country Work
0.13	0.20	0.20	18.0	0.39	1.31	8.9

Source: IMF, IEO calculations.

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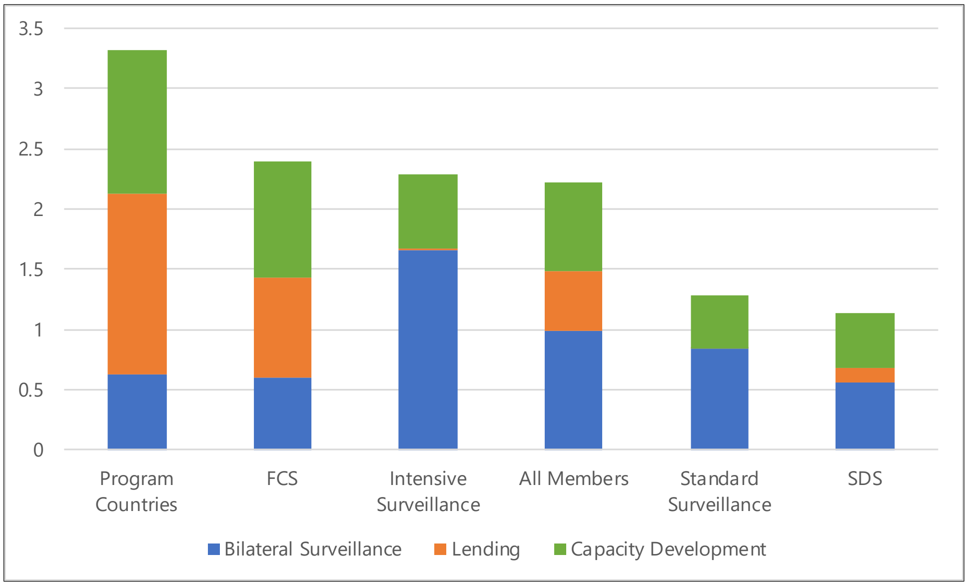
[10] Most SDS joined the IMF in the period 1963–89. Seven new SDS (including five microstates), or approximately a fifth of the current number, have become members since 1990.

[11] Size is not a criterion for Fund membership eligibility. Membership decisions are made by the Fund, which assesses whether an applicant (i) is a country with control over its territory, (ii) controls its external relations, and (iii) has the capacity and the will to fulfill its obligations as a member of the IMF.

[12] IMF members are generally PRGT eligible if their annual per capita GNI, based on the latest available qualifying data, is below the operational IDA cutoff ($1,175 in 2020). For SDS, this threshold is raised to twice the operational IDA cutoff, and to five times the operational IDA cutoff in the case of microstates.

12. In 2019, total IMF spending on SDS amounted to $38.9 million, just under 10 percent of the IMF's operational budget for country work, based on OBP data. Spending per SDS averaged approximately $1.2 million, compared to an average per member spending across the whole membership of $2.2 million and an average spending of $2.4 million per FCS (Figure 2). Compared to other countries SDS received a higher share of spending related to capacity development and a much lower share of spending related to program work.

Figure 2. IMF Average Spending Per Country, FY2019
(In millions of USD)



Source: IMF, IEO calculations.

Surveillance

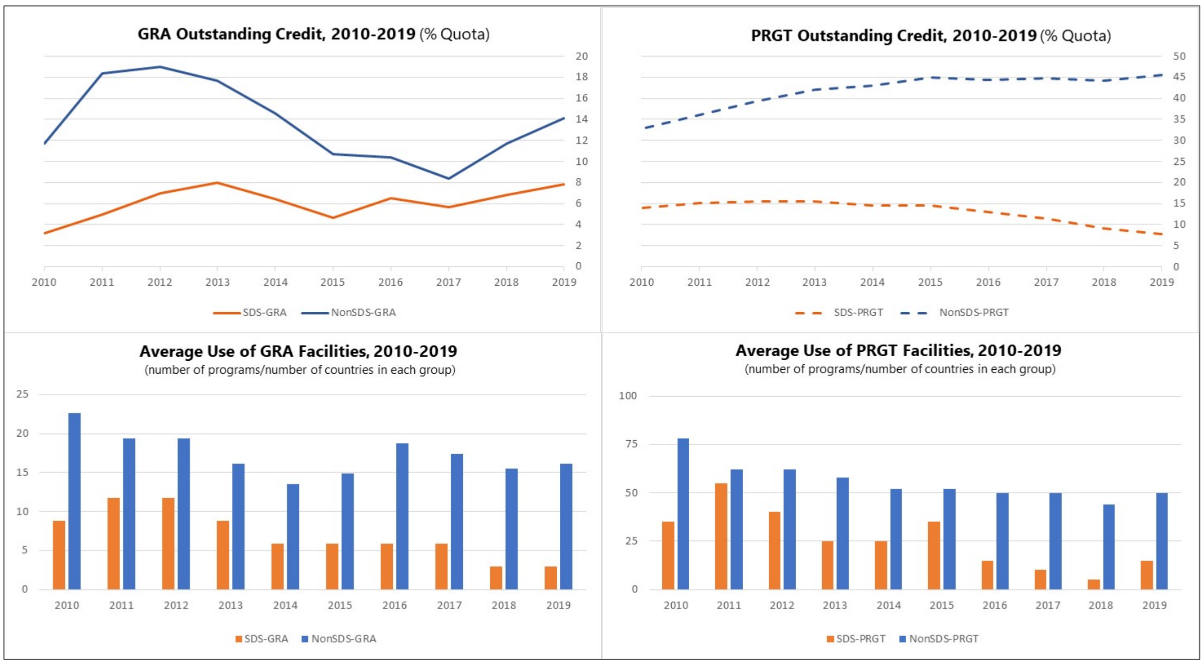
13. Currently, 23 out of 34 SDS are on an annual (i.e., standard) Article IV consultations cycle. The remainder (including six Pacific microstates and three countries with an IMF-supported program) are on a biennial cycle. Bilateral surveillance is supplemented with regional analyses and multilateral surveillance initiatives, such as the annual discussions with the Eastern Caribbean Currency Union (which also form part of the Fund's bilateral surveillance). While financial services contribute significantly to growth and employment in many SDS, just 10 FSAPs have been conducted for SDS since the FSAP was launched in 1999. In addition, a Financial Sector Stability Review (FSSR) has been conducted for two SDS.[13]

[13] The FSSR, created in 2017, is a donor-funded IMF TA instrument that combines a diagnostic review of the financial sector with capacity building to support sound financial sector reforms in low and lower-middle income countries.

Program support

14. Between 2010 and 2019, 56 percent of SDS were supported by IMF lending facilities or non-financing instruments at one time or another. Two-thirds of arrangements were supported through the PRGT (primarily the RCF, followed by the ECF and SCF).[14] The remaining one-third was roughly equally divided between support from the GRA (SBA, EFF, RFI, and ENDA) and non-lending instruments (two SMP, two PCI, and one PSI).[15] Over this period, the number of arrangements declined both under the GRA and the PRGT, and on average SDS used substantially less financial support from the IMF (as a percent of quota) than the rest of the membership (Figure 3). However, SDS were particularly intense users of the two emergency financing instruments, which are designed for rapid disbursement and do not involve ex post conditionality. The RFI and RCF were used by SDS on 9 occasions among 34 SDS, compared to 22 occasions among all 109 non-SDS low- and middle-income countries.

Figure 3. Small States Use of IMF Financing Facilities



Source: IMF, IEO calculations.
Note: SDS-GRA are those SDS not eligible for the PRGT. SDS-PRGT are those SDS eligible for the PRGT.

[14] The RCF and the RFI are fast-disbursing instruments with no ex post conditionality, intended to address BoP needs arising from natural disasters and other shocks. The ECF and the SCF provide assistance to PRGT-eligible countries with protracted and short-term balance of payments needs respectively.

[15] Staff Monitored Programs (SMP) involve no financing and are typically used to build a track record of policy performance to pave the way for use of Fund resources. Under an SMP, countries formulate a macroeconomic policy framework to be monitored by staff. SMPs are approved by IMF management, not by the Executive Board. The Policy Support Instrument (PSI) is another non-financing instrument offered only to PRGT-eligible countries as a signaling device of good economic performance to facilitate a country's access to external financing. The PSI requires Board approval. Similarly, the Policy Coordination Instrument (PCI) is a non-financing tool open to all members of the Fund that do not need financial resources at the time of approval.

15. SDS use of IMF emergency assistance surged in the first half of 2020 in response to the COVID-19 pandemic, alongside an explosion of use by other members. Between March 26 and June 1, 2020, the Executive Board approved 13 emergency financing arrangements (RCF, RFI, or a combination of both) for SDS, 1½ times the total registered in the previous 10 years (Table 3). At the same time, average access as a percent of quota more than doubled, as the IMF temporarily raised its access limit for these facilities. Thus far, emergency support has mainly been drawn by SDS in the Caribbean and Africa.

Table 3. Use of Emergency Facilities

	SDS		Non-SDS	
	2010–19	**2020**	**2010–19**	**2020**
Number of approvals	9	13	22	45
Caribbean	6	5	…	…
Pacific	2	2		…
African	1	4	…	…
Other	0	2	…	…
Frequency (num. programs/num. countries)	26.5	38.2	14.2	29.0
Total approved access (millions of SDR)	48	396	2,918	15,918
Average approved access (percent of quota)	42.22	92.31	35.77	78.04

Source: IMF, IEO calculations.

16. In addition to drawing on emergency financing, eligible SDS have also benefitted since April 2020 from additional forms of emergency relief: (i) grants from the Catastrophe Containment and Relief Trust (CCRT) for repayment of total debt service falling due to the IMF over the next six months; and (ii) the COVID-19 Debt Service Suspension Initiative (DSSI), an initiative by the G20, supported and implemented by the IMF and the World Bank, providing debt service suspension on official bilateral credit to the poorest countries, to manage the severe impact of the pandemic. Of five SDS eligible for CCRT grants, three (Comoros, São Tomé and Príncipe, and Solomon Islands) received debt service relief on April 15. As of May 25, 7 of 21 SDS eligible to benefit from the DSSI had formally requested to participate. In addition, the IMF is working closely with SDS country authorities, bilateral donors and other partners to identify opportunities to alleviate the impact of the pandemic on SDS.

Capacity development

17. Of the IMF's total spending on capacity development for all members of approximately $140 million in 2019, SDS received approximately $16 million, or 11 percent of total spending. In terms of average capacity development expenditure per member, each SDS received $466,000 on average, compared to $739,000 on average for each IMF member and $968,000 per FCS.

18. Regional Technical Assistance Centers (RTACs) play an important role in providing capacity development to SDS. Originally conceived to provide TA to small island economies, the first RTAC was opened in the Pacific in 1993 and the second in the Caribbean in 1999. These and other RTACs have been responsible for a growing share of all capacity development assistance to SDS, delivered both by resident advisors, who deliver TA and training throughout the region, as well as short-term experts.

19. In 2017, the Fund introduced the Climate Change Policy Assessments (CCPA) on a pilot basis. Undertaken jointly with the World Bank, CCPAs aim to provide an overarching assessment of countries' climate strategies and are meant to help countries build coherent macroeconomic frameworks for responding to climate change. All five CCPAs completed so far have been for SDS. A joint review of the CCPAs, by the Fiscal Affairs and the Strategy Policy and Review departments, is now underway.

Policy and research work

20. Until 2011, the Fund's policy and research work on SDS was largely on a bilateral or regional basis, with occasional research on collective challenges facing SDS. Since then, attention to the common challenges of this group of members has deepened, following increasing recognition of particular SDS challenges. This attention has led to a number of staff guidance notes and other policy papers, including a specific reference to SDS in the *2015 Guidance Note for Surveillance under Article IV Consultations*, as well as research and analytical papers on issues of particular concern to SDS (Box 1). The first guidance note on SDS was discussed by the Board in 2014. A revised and updated version was approved in 2017; it incorporated modifications to reflect Board papers and related Board discussions on SDS resilience to climate change and natural disasters and on changes in policies on access to Fund resources since 2014.

21. At the same time, area departments, especially Western Hemisphere Department (WHD) and Asia-Pacific Department (APD), also stepped up attention to SDS needs, preparing policy papers on specific macroeconomic, financial sector and other challenges facing these countries in each region. There has also been a steady flow of research work on small states, including several working papers. Topics include an analysis of rising public debt in many SDS and an estimation of fiscal multipliers for these countries and an examination of export diversification in LICs and SDS, exploring the potential linkages between export structure and economic growth and its volatility in LICs and small states.

Box 1. Main IMF Papers on Small States Since 2010

Staff Guidance Notes and other Policy Papers

- Staff Guidance Note on the Fund's Engagement with Small Developing States — May 24 (SM/14/66).
- 2017 Staff Guidance Note on the Fund's Engagement with Small Developing States — December 12, 2017 (SM/17/330).
- Macroeconomic Issues in Small States and Implications for Fund Engagement — February 20, 2013 (SM/13/43).
- Macroeconomic Developments and Selected Issues in Small Developing States — March 10, 2015 (FO/Dis/15/40).
- Small States' Resilience to Natural Disasters and Climate Change—Role for the IMF — November 7, 2016 (SM/16/313).
- Large Natural Disasters—Enhancing the Financial Safety Net for Developing Countries — April 11, 2017 (SM/17/76).
- Building Resilience in Developing Countries Vulnerable to Large Natural Disasters — April 4, 2019 (SM/19/68).

Area Department Papers

- Asia and Pacific Small States: Raising Potential Growth and Enhancing Resilience to Shocks — February 20, 2013 (SM/13/43 Sup. 1).
- Caribbean Small States: Challenges of High Debt and Low Growth — February 20, 2013 (SM/13/43 Sup. 2).

Selected Research Papers

- The Challenges of Fiscal Consolidation and Debt Reduction in the Caribbean - November 2012 (WP/12/276).
- Debt, Growth and Natural Disasters: A Caribbean Trilogy – July 2014 (WP/14/125).
- Enhancing Resilience to Natural Disasters in Sub-Saharan Africa (REO Chapter) — October 2016.
- Fiscal Policy Multipliers in Small States – August 2019 (WP/19/172).

Framework for engagement

22. The 2017 Guidance Note currently guides staff's engagement with SDS. It focuses on five main policy issues for IMF surveillance and program work organized within a framework called G.R.O.W.Th:

- *Growth and job creation:* the guidance note emphasizes that policies to strengthen growth and job creation are a priority. Staff teams should discuss growth issues for specific sectors and consult appropriately with other development partners. On job creation, the guidance note emphasizes that specific labor market institutions of SDS merit attention and that staff should investigate how public employment and public wages affect the labor markets.

- *Resilience to shocks*. The guidance note specifies that staff's macroeconomic analysis should give prominence to potential shocks, considering the appropriate balance between self-insurance, external insurance and private sector involvement in risk reduction.

- *Overall competitiveness*. The guidance note emphasizes that structural inefficiencies such as high energy and transportation costs, limited private sector development and labor market rigidities are key challenges to raising growth and improving competitiveness. Policy advice could cover facilitating domestic wage and price cuts, structural reforms, and consider the value of regional trade and cooperation for SDS.

- *Workable fiscal and debt sustainability options***.** Staff will need to find the appropriate balance of fiscal consolidation while promoting growth, particularly in heavily indebted countries.

- *Thin financial sectors*. Priorities highlighted in the guidance note include deeper financial sectors, more competition, better service delivery and strengthened oversight; and that SDS have been recently challenged by unintended consequences through the disruption of Correspondent Banking Relationships (CBRs).

23. The guidance note also:

- highlights the need for a strong focus on integrating risks emanating from natural disasters in Fund analysis of SDS and draws attention to the different tools and practices already developed in the IMF, including CCPAs, incorporation of adverse shocks from disasters in Debt Sustainability Assessments, consideration of the transmission of shocks through macro-financial linkages, and the need for buffers to cope with this type of vulnerability.

- provides a series of operational guidelines for surveillance and analytical work, including (i) the use of cross-departmental approaches to overcome resource and data constraints and improve the ability to extract lessons by broadening the geographical focus, (ii) encouraging analytical work with concrete policy implications, rather than basic research, and (iii) the provision to authorities of accessible economic policy tools to alleviate capacity limitations.

- recognizes that support for small states will need to involve other international institutions and development partners and should reflect the Funds' comparative advantage and the relative expertise of counterparts. It highlights that close collaboration between the Fund and partners should aim at ensuring consistent policy advice and would be particularly helpful when addressing regional challenges; and instructs staff to collaborate and remain closely engaged with partners on capacity development and to be cognizant of other IFI's constraints in dealing with SDS.

24. While all SDS are at least lower middle-income countries, debt sustainability assessments for 20 members are conducted using the IMF's Debt Sustainability Framework (DSF) for LICs, due to their eligibility to use PRGT resources. All remaining SDS are assessed using the IMF's Debt Sustainability Framework for Market Access Country (MAC-DSA). A review of the LIC-DSF in 2017 (IMF, 2017) identified particular weaknesses in DSF debt projections for SDS, with DSA's for more

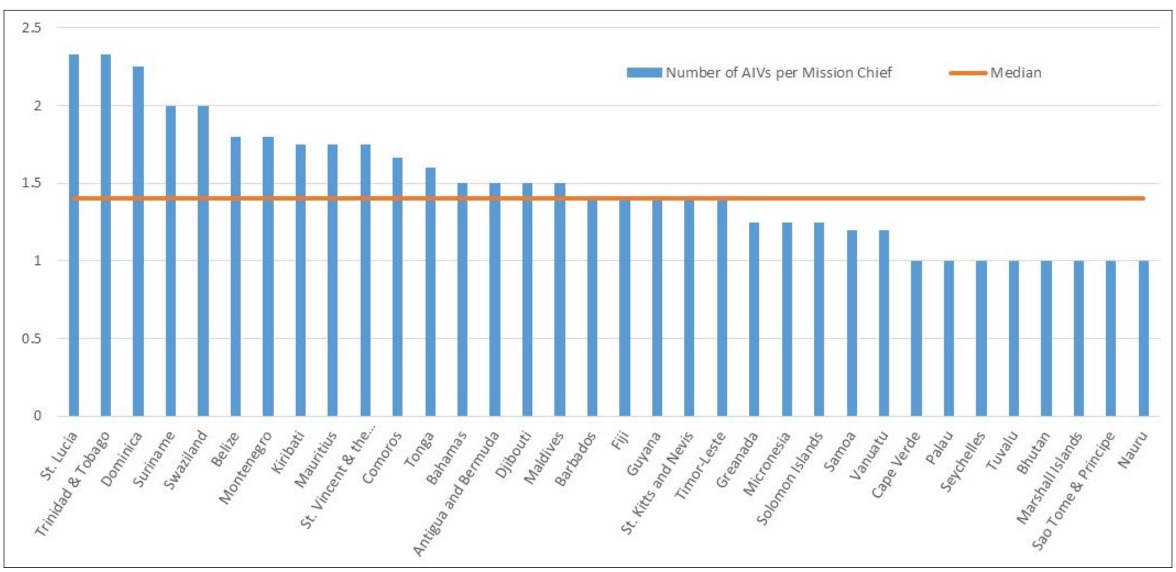
than half of all SDS between 2007-10 containing unexpected changes in debt over a 5-year horizon in excess of 15 percent of GDP. A general review of MAC-DSA is now underway.

Organization of work on small states

25. There is no single Fund-wide unit dedicated to work on SDS and currently country responsibilities for SDS are divided among several area departments (see Table 1). Approaches to organizing work on small states also differ across area departments. In Asia and Pacific Department (APD), country work on all 12 Pacific SDS is concentrated in a single "Small States" division. In the Western Hemisphere Department (WHD), SDS country work is distributed across three divisions, with one division clustering responsibility for the six members of the East Caribbean Currency Union. In the African Department (AFR), work on three SDS (Comoros, Mauritius, and the Seychelles) is conducted in one division (Eastern II), while separate divisions cover each of the three remaining SDS). Work on two other SDS is conducted in the European (EUR) (Montenegro) and Middle East and Central Asia Departments (MCD) (Djibouti). The Strategy and Policy Review department contributes to the coordination of the work on SDS through its policy work and facilitates knowledge-sharing across departments with a dedicated website.

26. Country teams working on SDS are typically smaller than those assigned to larger countries, turnover is quicker, and team members are often less experienced. Eight SDS had different mission chiefs for every Article IV consultation between 2010–19, while the median number of consultation cycles per mission chief was 1.4 over this period[16] (Figure 4).

Figure 4. SDS Mission Chief Turnover, 2010–19

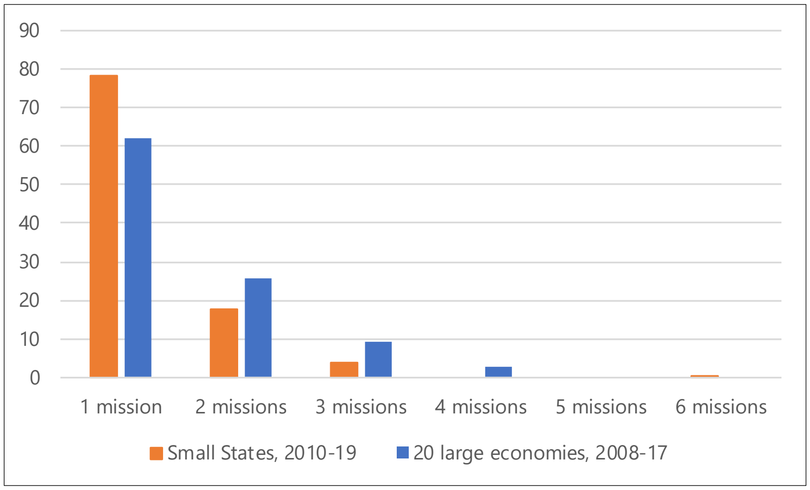


Source: IMF, IEO calculations.

[16] For comparison, in the sample used in the evaluation *IMF Advice on Capital Flows*, the median number of consultation cycles per mission chief was 1.6, and none of those countries had a different mission chief for every Article IV consultation. However, comparison of tenure between the groups based on this statistic is complicated to the extent that Article IV consultations are on average less frequent for SDS.

27. In regard to country teams, almost 80 percent of team members participated in only one Article IV mission in the period 2010–19 (Figure 5). For illustrative purposes, the comparable share for a sample of 20 larger advanced and emerging market economies in the period 2008–17 (IEO, 2019) was nearly 60 percent, an already high number.

Figure 5. Staff Participation in SDS Missions 2010–19



Source: IMF, IEO calculations.

IV. EVALUATION OUTLINE

Objective and coverage

28. The overarching goal of the evaluation is to consider how best the IMF can support its SDS members given these countries' distinctive vulnerabilities and needs and respecting the IMF's limited overall resource envelope. While most of the activity being evaluated will relate to the pre-COVID-19 pandemic experience, special attention will be paid to issues that now seem likely to be of particular importance going forward. Key tasks will be: (i) to assess whether existing approaches for the IMF's core operations—surveillance and policy advice, program support, and capacity development activities—are appropriate for the specific challenges facing SDS and whether particular circumstances merit a more granular approach for this country grouping; and (ii) to assess the institutional framework and procedures for the IMF's engagement with SDS, including its strategic approach, human resource management, and engagement with other development partners and institutional stakeholders. This evaluation could help identify steps to strengthen the quality, impact, evenhandedness, and effectiveness of future Fund engagement with these members and with others with similar challenges, including exposure to large climate change, natural disaster, and health-related shocks.

29. The evaluation will cover the 34 countries defined by the IMF as SDS. Country case studies will provide balanced coverage in terms of regional distribution, types of vulnerability, geographical characteristics, and size. The evaluation will focus on the period from 2010 to

June 2020, including the Fund's initial emergency response to the COVID-19 pandemic. For comparison, some aspects of the evaluation will also include data from the period 2000–10.

Evaluation questions – IMF core operations

Surveillance

(i) Was the IMF's advice to SDS in the context of surveillance—bilateral, regional, and multilateral—relevant, timely, and of good quality? Was advice appropriately tailored to country and regional circumstances and actionable? What was the value added and impact of SDS surveillance work?

(ii) Was Fund advice to SDS consistent with staff guidance notes and other Fund policy documents? How well did the internal review process for the Fund's advice work in country cases? Were relevant outside views taken into account?

(iii) Has overall guidance on IMF surveillance on SDS been appropriate and effective? Were lessons learned from experience and incorporated in guidance notes? Was policy advice consistent and evenhanded across regions and countries?

(iv) What factors affected the effectiveness of IMF surveillance on SDS and how did the Fund respond? Was the quality and timeliness of data on SDS adequate for Fund's work?

(v) How well does the Fund's framework for bilateral surveillance fit the special circumstances of small states? Would different approaches help to increase overall quality?

(vi) How well did specific surveillance tools, such as the Debt Sustainability Frameworks for Low-Income Countries and for Market Access Countries work in the SDS context?

(vii) Were macro-financial issues, including AML/CFT and ITAFF related questions, properly integrated in SDS' surveillance?

(viii) Was IMF policy advice to SDS consistent and harmonized with that of external partners?

Program support

(ix) Was program support to SDS relevant, timely, and well structured? Was it well tailored to their specific circumstances? In the specific case of the COVID-19 pandemic, were the speed of, amount, and conditions associated with the Fund's response adequate, taking into account both the needs of SDS and the Fund's institutional rules and constraints?

(x) Were the outcomes of IMF financial support consistent with expectations? If not, what factors prevented achievement of these and how did the IMF respond? How catalytic has Fund financing been in SDS?

(xi) Are the Fund´s lending facilities and non-lending instruments well suited to meet the needs of SDS? Are they sufficient to alleviate the effects of the different types of natural disasters? What factors explain the relatively low recourse to non-emergency types of IMF financing by SDS?

(xii) How did financing provided by the IMF dovetail with that of other donors? Was the IMF effective in the context of discussions within the broader international community on the overall financing needs of SDS?

Capacity development

(xiii) Were CD activities relevant, timely, and of good quality? Were they sufficiently tailored to country needs and the specific circumstances of each case, including absorptive capacity?

(xiv) What have been the relative strengths and weaknesses in delivering of CD to SDS? How effectively have particular challenges posed by geographical distance and the disruption to travel from the COVID-19 pandemic been addressed?

(xv) Were CD initiatives appropriately integrated with the IMF's surveillance and program-related priorities?

(xvi) How effectively were IMF CD activities coordinated with other CD providers? How useful were collaborative CD initiatives, including the pilot CCPAs and assistance provided by RTACs, for SDS?

Evaluation questions – framework and procedures

Strategic framework

(xvii) Has the IMF's strategy for engagement in SDS been clear and effective? Has the Fund's definition of SDS been useful and adequately operationalized?

(xviii) What are the objectives, priorities, mandate and expectations of the membership regarding the role of the IMF in SDS? Are these sufficiently clear and well understood?

(xix) Have the institutional mechanisms for IMF engagement with SDS, including institutional structures and budgetary resources, been appropriate to achieve these objectives?

(xx) How effective has been the role and guidance of the Executive Board and the Management team regarding SDS?

(xxi) Were adequate mechanisms for knowledge and experience sharing across departments and country teams in place?

Staffing issues

(xxii) Have staff resources been appropriately allocated to SDS (as a whole, across regions, and to individual members), taking account of their special needs and the multiple competing needs for scarce resources? What factors influenced the allocation of staff resources, both between SDS and non-SDS, and among SDS?

(xxiii) What factors affected staff's incentives to work on SDS? Were these managed appropriately?

(xxiv) Did IMF staff working on SDS possess the adequate expertise/training to deal with the distinct challenges of these countries? If not, how did the IMF address this gap?

(xxv) Did the turnover of staff assigned to SDS reflect an appropriate balance between the special needs of these members and the Fund's institutional constraints?

Engagement with external partners and other stakeholders

(xxvi) Were the IMF's interactions with partners and external stakeholders in working on SDS issues effective and sustainable?

(xxvii) In the specific case of the COVID-19 pandemic, was the Fund's response in establishing or strengthening engagement and cooperation with partners on SDS concerns timely, adequate and effective?

(xxviii) Would there be value in developing new frameworks to enhance collaboration on SDS?

V. METHODOLOGY AND EXPECTED OUTPUT

30. The main information sources will be desk reviews and analysis of IMF documents—policy papers, research papers, surveillance and program documents—and interviews of (i) IMF staff—at headquarters, in regional technical assistance centers, and in SDS; (ii) country authorities and other local stakeholders, (iii) SDS bilateral, regional and multilateral partners; and (iv) other international organizations. Ideally, interviews will be in person, but travel constraints could require extensive use of virtual meetings. Interviews will be complemented with surveys of IMF staff and country authorities.

31. The evaluation will combine detailed country case studies for a representative group of SDS, covering both surveillance-only and members with IMF-supported programs and users of

IMF emergency assistance, including to deal with the COVID-19 pandemic, together with a number of cross-cutting thematic studies. Together with the main report, the evaluation will include the following background papers:

Country case studies

- *Four Caribbean country case studies*. The paper (and similar papers for Pacific, African and other SDS (below), will assess the Fund's role in helping these countries face their specific vulnerabilities and challenges, highlighting relevant issues at the regional level.

- *Four Pacific country case studies*.

- *Four African and other country case studies.*

Thematic papers

- *Growth and competitiveness*. The paper will review the specific growth-related challenges of SDS and will assess value added and impact of Fund work to relieve growth constraints and foster competitive, diversified economies. Such issues take on additional importance given the likely sustained damage from the COVID-19 pandemic to the tourism sector that has been a principal foreign exchange earner for many SDS.

- *Climate change and natural disasters*. The paper will assess to what extent the Fund's engagement—through surveillance, program support, and capacity development work—has helped SDS build resilience and access other sources of financing. It will review the experience with Disaster Resilience Strategies, the five initial CCPAs and the COVID-19 pandemic. and will assess the extent to which Fund analysis and advice helped to catalyze climate change financing.

- *Fiscal policy and debt*. Issues to be covered include the Fund's advice on fiscal and debt sustainability while promoting growth, particularly in SDS facing increasingly difficult debt situations; the extent to which debt resolution strategies have taken account of SDS specific needs, circumstances and administrative capacities; and the effectiveness of the evolving LIC and MAC debt sustainability frameworks for SDS.

- *Financial sector issues*. The paper will assess the Funds' role in supporting deepening of financial sectors in small states, including by supporting policy makers' efforts to promote competition, foster financial stability and achieve efficient scale in financial sector activities. It will also assess Fund's efforts to advise and assist SDS strengthen legal frameworks for financial services and improve compliance with international AML/CFT standards and in addressing emerging financial sector challenges, including disruption of correspondent banking relationships.

- *Capacity development*. The paper will review the IMF's work on capacity development in SDS at both the bilateral and regional levels. It will cover, inter alia, the demand and supply constraints facing CD delivery for SDS, the adequacy of the various forms of delivery, particularly in the face of more difficult travel, and coordination with other providers.

- *Staffing issues*. The paper will analyze how the IMF's human resources policy and practice affect staffing for work on SDS. It will study staff members' professional profile, interests, and incentives to work on SDS as well as the Fund's institutional needs and constraints, including the allocation of resources and the length of assignments.

- *Collaboration with partners*. The paper will assess the relevance, efficiency, and effectiveness of IMF collaboration with partners in its engagement with SDS. It will also examine whether lessons from collaboration can inform IMF engagement with partners more broadly across the membership.

32. **Indicative timeline** (subject to further developments related to the COVID-19 pandemic):

(a) Informal Board Seminar on the Issues Paper (to be conducted in written format or via virtual meeting): July 2020.

(b) Tentative target date for Board discussion: December 2021.

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