

Background Material on the Evolution of IMF Policies on Prolonged Use

This annex provides additional information to support the discussion in Chapter 3.

Evolution of the IMF's Attitude to Prolonged Use

On several occasions in past decades, the Executive Board recognized that adjustment often required a longer time frame than implied by existing UFR policies¹ and, in response, instituted new modalities of UFR. These new policies were initially conceived as short term and temporary, out of concern to preserve the monetary nature of the IMF and the revolving character of its resources, but they ended up being renewed year after year. Until the early 1990s, these guiding principles were thought to apply equally to the use of the IMF's general and concessional resources.² Thereafter, the policies applied to the two groups diverged, and there was a gradual acceptance of a greater degree of prolonged use of concessional resources while giving renewed emphasis to the revolving character of the IMF's general resources.³

¹Initially, IMF financing in the upper credit tranches was typically provided under a Stand-By Arrangement, whose normal period is one year. It may extend up to but not beyond three years in appropriate cases (Executive Board Decision No. 6056-(79/38) of March 2, 1979). Since 1978, obligations incurred under a Stand-By Arrangement must be repaid within a period of 3¼ to 5 years.

²For example, EBS/91/108, "Selected Operational Issues Related with the Use of Fund Resources" explicitly notes that the principle of the revolving character of the IMF's resources must be applied consistently to general and concessional resources, and does not distinguish between the two in the remedial actions it suggests to deal with prolonged use.

³The Executive Board reviewed prolonged use on several occasions during the 1980s, starting in 1984. The last comprehensive review of prolonged UFR was discussed by the Board in 1991. Thereafter, the issue was not put on the Board's agenda until 2000, where prolonged use was discussed only as a background issue to the review of IMF facilities.

Prolonged use of the IMF's general resources

The official interpretation of the IMF's mandate initially emphasized the temporary nature of the support that the IMF could provide to its members: "The authority to use the resources of the Fund is limited to use in accordance with its purposes to give temporary assistance in financing balance of payments deficits" and "the task of the Fund is to help members that need temporary help. The Fund's attitude toward the position of each member should turn on whether the problem to be met is of temporary nature and whether the policies the member will pursue will be adequate to overcome the problem within such a period."⁴

The creation of the EFF in the wake of the first oil shock marked the first important departure from the original conception. However, the wording of the decision made it clear that this departure was intended to be the exception, not the rule: the EFF was to be used in special circumstances, including where a member suffered serious payments imbalances relating to structural maladjustments and where it was expected that the needed improvement in the balance of payments could only be achieved over an extended period. Subsequent developments, which included an increasing use of series of one-year SBAs and the institution and prorogation until 1992 of the enlarged access policy, ensured that the use of the EFF indeed remained exceptional, although not the recourse to IMF resources for a more prolonged period of time than implied by the original interpretation of the IMF's mandate.

⁴Executive Board Decisions No. 71-2 of September 26, 1946 and No. 102-(52/11) of February 13, 1952, respectively. The "Guidelines on Conditionality" adopted in 1979 further stated that: "The normal period for a stand-by arrangement will be one year. If, however, a longer period is requested by a member and considered necessary by the Fund to enable the member to implement its adjustment program successfully, the stand-by arrangement may extend beyond the period of one year. This period in appropriate cases may extend up to but not beyond three years." (Executive Board Decision No. 6056-(79/38) of March 2, 1979.)

The 2000 Executive Board discussion of the “Review of Fund Facilities” marked a sharp reversal of attitudes toward prolonged UFR. On this occasion, a number of Board members expressed concern “that some members may rely unduly on Fund financial assistance in place of seeking market financing, and saw a need to review the Fund’s policies in this connection.”⁵ These concerns led to the introduction of repurchase expectations⁶ and of surcharges on outstanding obligations to the IMF in excess of normal access (i.e., 100 percent and 300 percent of a member’s quota). While primarily aimed at providing an incentive against large use of IMF resources, this measure was also presented as an indirect incentive to avoid prolonged use, to the extent that it is associated with rising outstanding obligations.

Prolonged use of the IMF’s concessional resources

Beyond the concessionality of the loans attached to it, the main innovation brought about by the ESAF was the relaxation of the requirement that lending arrangements should solve entirely members’ balance of payments problems. Instead, programs supported by the ESAF were required only to “assure substantial progress during the three-year period toward an overall position and structure of the balance of payments that is consistent with orderly relations with creditors and a reduction in restrictions on trade and payments, while permitting the timely servicing of obligations to the Fund” (EBM/87/171). The ESAF being initially conceived as a one-off operation, the decision was ambiguous, to say the least, as to how the unfinished agenda should be tackled in the post-ESAF period.

Between 1990 and 1997, the ESAF was gradually transformed through a series of steps into a permanent facility without any restrictions on the number of arrangements that an eligible member could enter into. In late 1990, the ESAF Trust Instrument was amended so as to allow *one additional annual arrangement* at the expiration of the initial three-year ESAF arrangement, although only where performance had been satisfactory and within unchanged overall access limits. In 1992, the Board opened the possibility of renewing ESAF support through a *single one- or two-year arrangement*, when the three-

year commitment period had expired with undrawn amounts. Then, in 1993 the Instrument was amended again to allow for a second three-year arrangement, which could itself be followed by a single annual arrangement. This option was to be available only for good performers with appropriately strong adjustment programs. In 1995, the ESAF became a self-sustaining facility, offering eligible members indefinite access to concessional resources, though each member would remain bound by the limits set in 1993 regarding the number of arrangements and the “good performance” test. In 1997, these last limits were lifted.

These successive extensions were agreed upon only after protracted negotiations, due to the reluctance of a minority of Directors to legitimize prolonged use of the IMF resources, even concessional ones. The need to reflect these different perspectives led the Board as a whole to emphasize that the purpose of these successive extensions was *not to provide a source of continuous financing for individual countries*, but rather to maintain the Fund’s ability to respond to members’ needs as they arise.⁷ Apart from the factors mentioned in Chapter 3, this decision also reflected a third, “defensive lending” motivation: ensuring a smooth repayment by the countries with the heaviest debt-service ratios to the IMF.⁸

Evolution of the Strategy Vis-à-Vis Prolonged Use

Program design elements

From 1984 to 1991, reviews of prolonged use put a strong emphasis on improvements in program design and implementation to address prolonged use, each of the reviews essentially building on the previous ones and increasing the specificity of its recommendations. By contrast, the 2000 review, which tended to downplay the importance of prolonged use, did not suggest any specific remedy related to

⁵See Chairman’s summing up (BUFF/00/41).

⁶For purchases in the credit tranches and under the CFF, the expectation schedule starts one year in advance of the obligation schedule, beginning 2¼ years after a purchase and ending after 4 years. For the EFF, the expectation schedule begins after 4½ years, as with the obligation schedule, but repurchases are to be doubled, such that the expectation schedule will end after 7 years rather than 10 years under the obligation schedule.

⁷See Chairman’s summing up of EBM/97/5, EBM/97/8, and EBM/97/10.

⁸The then Managing Director put the case in the following terms: “I would suggest that these few cases could appropriately be addressed through the continued availability of concessional ESAF resources on present terms” [as opposed to extending to them one further round of ESAF arrangements with a 20-year maturity, as proposed by the U.K. Chancellor of the Exchequer]. “Through this instrument, the Fund would have the possibility of tailoring its financing to the individual situation of each member, *extending for the period needed—in a few cases through several successive ESAF arrangements—the concessional financing required . . . , while avoiding significant humps in net transfers from the member to the Fund.*” (BUFF/95/31.)

program design, nor did it recall or call for the implementation of the measures endorsed in previous reviews.

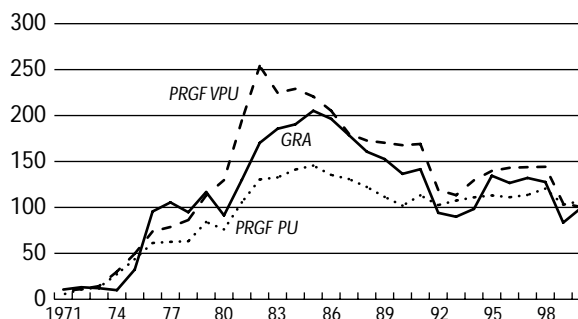
Access to IMF resources

The majority view of the Executive Board regarding access has consistently been that it would not be appropriate to introduce strict rules limiting access based on the frequency or length of UFR, because even perfect implementation might fail to deliver the desired balance of payments outcome. However, the policies adopted in 1983/84 on the use of general resources made it clear that access should be reduced over time and that past performance in using the IMF's resources should be taken into account in the determination of further access.

While these policies were not applicable ipso facto to concessional resources, the decisions adopted by the Board from 1990 onward left little doubt that the guiding principles of access policy were similar for both categories of resources. In 1993, the Board decided that "for repeat users, access would take into account the amount of the member's outstanding use of Fund credit and its record in using Fund resources. . . . This would signal the need to phase out the reliance on exceptional balance of payments financing" and "ensure that even with continued availability of the ESAF, individual members would, over time, phase out their reliance on ESAF support."⁹ In 1995, the Board further specified that "lower (or no) access may be appropriate in the case of . . . countries that have relatively weak track records and are not able to implement sufficiently strong policies . . ."

Our case studies suggest that the justification of the level of access proposed in staff reports was treated in a rather perfunctory manner. This eventually caused the Executive Board in July 2000 to ask for a revision of the operational guidelines calling on staff to provide more detailed justifications of access proposals. As regards the evolution of the level of access, only about one-fifth of prolonged users with more than one three-year ESAF/PRGF arrangement had a consistently diminishing access. A similar proportion had access that actually increased over time. The remainder had access that either was stable over time or diminished only between the first and second three-year arrangement, and remained broadly stable thereafter. Among GRA arrangements, since 1990, 43 percent of prolonged users had higher annual access in their most recent (or last) arrangement than in their first, and just over a fifth had a consistently

Annex Figure 2.1. Average Outstanding Obligations of Prolonged Users to the IMF
(In percent of quota)



Sources: IMF Treasurer's Department and IEO calculations.

Note: In this figure, prolonged users are treated as a fixed group, consisting of the countries listed in Chapter 2. However, the broad trends are not very sensitive to the precise composition. Not every country in this sample was a prolonged user in each year. The choice of the fixed rather than the dynamic definition in this case was dictated by concerns not to understate the decline in outstanding obligations of the group of prolonged users. VPU: very prolonged users.

diminishing annual access. Another way to capture the lack of consistent implementation of access guidelines is to look at the evolution of prolonged users' outstanding obligations to the IMF over time (see Annex Figure 2.1). The general trend is fairly consistent both within and across groups: outstanding UFR declined sharply in the second half of the 1980s, but then remained fairly steady during the 1990s.¹⁰

Strengthened analytical and assessment efforts

In 1990, the Executive Board approved the proposal to include in any new UFR request a systematic review of experience under preceding arrangements. In 1995, the Board went a step further by recommending stock-taking, on a case-by-case basis, toward the end of the three-year arrangement, to reflect on what has been achieved and how to ensure strong performance in a subsequent arrangement (i.e., without necessarily waiting for a new UFR request to arise).¹¹

¹⁰The step declines observed in 1981, 1993, and 1999 partly reflect the impact of general quota increases. It should be noted that if access is reduced very gradually, disbursements may exceed repayments for a relatively long period, especially under concessional facilities, thus causing outstanding obligations to increase for a while even though access itself is being reduced.

¹¹See BUFR/90/37 and BUFR/95/95 for the acting Chairman's summing up of the relevant Board discussions.

⁹EBS/93/32, "Operational Modalities and Funding Alternatives for an ESAF" and EBS/95/130, "Continued Financing and Adaptation of the ESAF."

Exit strategies

Evidence from the case studies again suggests that the recommendation that staff reports should provide medium-term balance of payments projections and attempt to foresee a reasonable timetable for the disengagement of the IMF was often not followed. For example, medium-term projections for the Philippines in the 1994 EFF projected financing gaps even after market access had been restored. Part of the problem was the lack of clear criteria for a balance of payments financing gap in cases where countries had access to private financial markets. By contrast, in Pakistan and Senegal, most medium-term projections showed no financing gap beyond the program period, but such projections proved unrealistic.

As concerns the use of strengthened surveillance in the post-program period, the emphasis put by the 2000 “Review of Fund Facilities” on post-program monitoring essentially just formalized a preexisting disposition. While all GRA arrangements have a consultation clause stating that, under certain conditions, members shall consult with the IMF after the expiry of the arrangement “at the request of the Managing Director,” the facilities review instituted a presumption that countries with obligations to the IMF exceeding 100 percent of their quota at the expiration of the program would undergo this procedure for as long as their outstanding liabilities to the IMF exceeded the threshold.

For users of concessional resources, the principle of post-program monitoring as a means of avoiding prolonged use of ESAF resources was formally established in the early 1990s. In considering operational details for an ESAF successor, the Board endorsed the suggestion of “post-ESAF enhanced consultations and program monitoring . . . on a limited transitional basis, in cases where the macroeconomic situation remains vulnerable and the authorities perceive benefits

in a continued close policy dialogue with the IMF.¹² Subsequently, it was also envisaged that one option for continued IMF support for the programs of former ESAF users that ceased to have a need for IMF financing would be through precautionary arrangements: “Directors considered that . . . a precautionary arrangement would signal the Fund’s approval of the country’s adjustment program, thereby catalyzing financial support from other sources, while providing assurances that Fund resources would be available should the country’s circumstances change. Directors were persuaded, however, by the arguments against granting precautionary ESAF arrangements. They broadly agreed that ESAF-eligible countries without a recurrent or prospective balance of payments need could instead request a precautionary extended arrangement, which could be replaced or supplemented by an ESAF arrangement in the event that a balance of payments need emerged.”¹³

The implications of this exit strategy for other creditors were spelled out rather bluntly in 1991, when a staff report noted that: “In cases where external viability is not in reasonable prospect . . . the Fund could provide support in the early stages of the adjustment process . . . to help ensure the establishment of an appropriate macroeconomic framework. However, other creditors may have to continue their contributions, in part to facilitate repayments to the Fund, and there would need to be a clear acknowledgement by creditors of the revolving character of the Fund’s resources.”¹⁴

¹²“Operational Modalities and Funding Alternatives for an ESAF Successor—Preliminary Considerations” (EBS/93/32).

¹³Chairman’s summing up of EBM/98/73 on “Distilling the Lessons from the ESAF Reviews.”

¹⁴“Selected Operational Issues Related with the Use of Fund Resources” (EBS/91/108).