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Independent Evaluation Office
of the International Monetary Fund

BACKGROUND PAPER

BP/25-01/04

IMF Advice on Fiscal Policy—Selected Issues

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ABBREVIATIONS

AE	Advanced Economy
AFR	African Department (IMF)
APD	Asia and Pacific Department (IMF)
CPIA	Country Policy and Institutional Assessment
DMF	Debt Management Facility
EFF	Extended Fund Facility
EM	Emerging Market
EMDE	Emerging Market and Developing Economy
EMMIE	Emerging Market and Middle-Income Economy
EU	European Union
EUR	European Department (IMF)
FAD	Fiscal Affairs Department (IMF)
FM	Fiscal Monitor
FCS	Fragile and Conflict-affected State
GDP	Gross Domestic Product
GFC	Global Financial Crisis
GFS	Government Finance Statistics
GFSR	Global Financial Stability Report
HIPC	Heavily Indebted Poor Country
IADB	Inter-American Development Bank
ICD	Institute for Capacity Development (IMF)
LIC	Low-Income Country
LIC-DSF	Debt Sustainability Framework for Low-Income Country
MAC DSA	Debt Sustainability Assessment for Market Access Countries
MCD	Middle East and Central Asia Department (IMF)
MCM	Monetary and Capital Markets Department (IMF)
MDRI	Multilateral Debt Relief Initiative
MTDS	Medium-Term Debt Management Strategy
NATO	North Atlantic Treaty Organization
OECD	Organization for Economic Co-operation and Development
PFM	Public Finance Management
R&D	Research and Development
REO	Regional Economic Outlook
RRDC	Resource Rich Developing Country
SPR	Strategy, Policy and Research Department (IMF)
SIPRI	Stockholm International Peace Research Institute
SRDSF	Sovereign Risk and Debt Sustainability Framework for Market Access Countries
TA	Technical Assistance
WEO	World Economic Outlook
WHD	Western Hemisphere Department (IMF)

CHAPTER 1—IMF TOOLS AND ANALYSIS UNDERPINNING FISCAL POLICY ADVICE, 2008–23

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

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EXECUTIVE SUMMARY

Over the past 15 years, the IMF has shown notable intellectual agility and institutional adaptability in advancing fiscal policy advice. In the aftermath of the Global Financial Crisis, the Fund moved beyond its traditional focus on fiscal sustainability to recognize the critical roles of fiscal policy in stabilizing output and supporting long-term growth. This evolution reflected a strong commitment to evidence-based policymaking, openness to revising established views, and sustained analytical innovation. The Fund's research helped shape global debates on fiscal consolidation, the implications of "low-for-long" interest rates, and the fiscal dimensions of climate change and inequality—often positioning the institution as an intellectual leader among international financial organizations.

Analytical progress was matched by important operational advances. The development of the Sovereign Risk and Debt Sustainability Framework (SRDSF), the Fiscal Space Framework (FSF), and FAD's optimizing models enhanced the rigor, transparency, and empirical grounding of fiscal assessments. Complementary realism tools embedded in these frameworks strengthened the credibility of projections by disciplining overly optimistic assumptions, while new methodologies—such as the Public Sector Balance Sheet, Fiscal Risk Assessment Tool, and Debt-at-Risk framework—broadened the coverage of vulnerabilities beyond traditional debt indicators. These innovations, supported by extensive research on fiscal multipliers, spillovers, and the distributional effects of fiscal measures, have provided a more comprehensive basis for tailoring fiscal advice to country circumstances.

Despite these advances, several analytical and operational gaps remain. Methodological transparency and replicability are uneven, limiting external scrutiny and the accumulation of cumulative knowledge. Empirical work remains heavily concentrated on advanced economies, leaving weaker guidance for countries with different transmission mechanisms and financing structures. Moreover, existing analytical toolkits still fall short of addressing several foundational questions—how to calibrate the fiscal–monetary policy mix under normal conditions, how to select desirable medium-term debt anchors from among feasible options, and how to quantify the long-run fiscal implications of investment, redistribution, and climate policies. Liquidity risks, though more systematically incorporated into the SRDSF and LIC-DSF, are not yet fully integrated across frameworks. Similarly, the IMF's growing work on inequality, defense, and climate adaptation has not been consistently embedded within debt sustainability analysis or medium-term fiscal planning. Addressing these gaps would strengthen the coherence and evenhandedness of IMF fiscal advice and ensure that analytical innovations translate more fully into operational guidance.

I. Introduction

1. **The Fund's approach to fiscal policy is framed around three core goals: safeguarding fiscal sustainability, stabilizing output over the cycle, and raising potential output through the provision of public goods.** Fiscal sustainability has both a solvency dimension—ensuring that public debt remains on a sustainable path—and a liquidity dimension—ensuring governments can meet gross financing needs as they arise. Macroeconomic stabilization requires fiscal policy to operate countercyclically where possible, supporting demand during downturns and withdrawing stimulus in booms, in coordination with other macroeconomic policies. Raising potential output through the provision of public goods is achieved through measures that expand infrastructure and human capital investment, strengthen institutions, and advance broader priorities such as the Sustainable Development Goals (SDGs) and the green transition. The adoption of institutional strategies on social protection, climate change, and gender (IMF, 2019a; 2021a; 2022a) has further elevated the importance of synergies and trade-offs between financing these long-term objectives and fiscal sustainability.

2. **This chapter reviews the analytical contributions and tools developed by the IMF to inform fiscal policy advice across the three objectives.** The emphasis is on the tools themselves—their conceptual foundations, empirical design, and practical features—while their application by country teams or integration into flagship publications is addressed in other background papers.[1] References to surveillance practice are included only where they help illustrate a tool's operational value or limitations. The chapter focuses on macro-fiscal tools used in the surveillance context, while noting that some are also applied in program work. It covers aspects of expenditure and tax composition relevant for macro-fiscal analysis, but excludes more structural issues—such as pension and health reforms, or the efficiency and incentive effects of specific taxes and spending programs—that lie beyond its scope.

3. **This chapter reviews key innovations in IMF research and assesses their incorporation into toolkits that support country teams.** Reflecting the Fund's scientific culture, staff research has played a central role in shaping fiscal policy doctrines and recommendations (Ban, 2015; and Ban and Gallagher, 2015). The discussion is organized around the three thematic areas outlined above: (i) fiscal sustainability, including fiscal risk and fiscal space; (ii) fiscal policy for output stabilization; and (iii) fiscal policy to support potential output and the provision of public goods. Particular emphasis is placed on how these tools help operationalize trade-offs among competing fiscal objectives, clarifying when they reinforce one another and when tensions arise. In doing so, the chapter highlights the value of IMF toolkits in disciplining staff assessments and guiding the allocation of fiscal space in ways that balance short-term stabilization needs with long-term development goals.

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[1] A recurring challenge in the design and application of fiscal analytical tools is the uneven availability and quality of data, particularly in LICs. These limitations—ranging from gaps in coverage and timeliness, insufficient detail in fiscal classifications, lack of transparency around off-balance-sheet items, and the scarcity of high-frequency macroeconomic data—constrain the use of advanced methodologies and tend to bias tools toward the circumstances of advanced economies.

II. FISCAL SUSTAINABILITY

4. **This section reviews the IMF's analytical work and operational toolkits for assessing debt sustainability, fiscal space, and fiscal risks, and explains how these inform fiscal advice.** We proceed in four steps. First, we review the IMF's research and operational frameworks on debt sustainability and sovereign risks—including the SRDSF for market-access countries and the LIC-DSF for low-income countries—highlighting their treatment of debt-carrying capacity, the implications of shifting interest-growth differentials, their core modules (solvency, liquidity, and risks at various horizons), the evolution of realism tools, and remaining analytical gaps. Second, we turn to complementary instruments: the Fiscal Space Framework (FSF), which provides a standardized approach to gauging room for policy support, and balance-sheet-based and risk tools—such as the Public Sector Balance Sheet database and Debt-at-Risk—that broaden coverage of vulnerabilities. Box 1 provides further details on the FSF.

Debt Sustainability and Sovereign Risks

5. **IMF research has explored how macroeconomic and structural factors influence a country's debt-carrying capacity.** Analytical work has assessed member countries' ability to sustain higher debt-to-GDP ratios, quantified the fiscal adjustments required to reverse debt surges, and evaluated whether changes in debt trajectories are needed to meet long-term financing needs. Flagship publications have also explored the determinants of debt sustainability, including the implications of declining interest–growth differentials (e.g., Ghosh and others, 2013; October 2016 and April 2017 Fiscal Monitor (FM)) and the feedback effects of debt levels interest and growth rates (Box 2).

6. **Completing this research, the IMF has developed tools to support staff assessments of debt sustainability and risks of debt distress.** Since 2002, different frameworks have been applied to market-access countries (MACs) and low-income countries (LICs), reflecting their distinct characteristics. These tools have evolved significantly, and current versions include modules that assess short-, medium-, and long-term debt risks under various macroeconomic and policy scenarios.

7. **The DSA framework for MACs has evolved considerably, most recently with the introduction of the Sovereign Risk and Debt Sustainability Framework (SRDSF) (IMF, 2021b; 2022b).**[2] The SRDSF provides two outputs: a sovereign risk assessment and a debt sustainability assessment. These assessments aim to capture vulnerability to sovereign stress events, risks that debt could become unsustainable, and prospects for stabilizing the debt trajectory in the baseline scenario. Analytical modules assess sovereign risks across three horizons. In the near term, an early warning system estimates the likelihood of sovereign stress

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[2] While DSAs had long been standard practice for LICs, they were not systematically used in fiscal analysis for advanced economies before the GFC. Recognizing this gap, the Fund introduced a DSA framework for market access countries (MAC DSA) in 2002, refined it in 2011, and ultimately replaced it with the SRDSF in 2021 (IMF, 2022b).

over a one-to two-year horizon. Medium-term risks are evaluated through: (i) the debt fanchart module, which assesses solvency over a five-year horizon; (ii) the gross financing needs module, which gauges liquidity pressures and the country's ability to meet its gross financing needs over the medium term; and (iii) stress tests for country-specific vulnerabilities, including contingent liability shocks. Long-term modules are used to capture structural risks, such as those related to climate change, demographics, and natural resource depletion.

Box 1. Measuring "Fiscal Space" in IMF Surveillance

Background

The concept of fiscal space—understood as a government's ability to raise spending or cut taxes without endangering debt sustainability or macroeconomic stability—has long informed IMF work (Heller, 2005). Earlier approaches to measuring fiscal space included: (i) fiscal gap indicators, based on medium-term debt stabilization paths; (ii) assessments of whether debt and deficits are "stationary" over time; and (iii) intertemporal budget constraint models incorporating macro-fiscal feedbacks (IMF, 2012). Each approach has strengths, but also limitations, including reliance on mechanistic assumptions or backward-looking indicators.

To improve rigor and consistency in its fiscal advice—particularly following the GFC—the IMF introduced a formal *Fiscal Space Framework* (FSF) in 2016 (IMF, 2016a). The tool defines fiscal space as the ability to provide stimulus without compromising debt sustainability or macroeconomic stability. Initially piloted in 38 advanced and emerging economies, it was extended to 31 additional countries (including some LICs with market access) in 2018 and is encouraged for all countries covered under the SRDSF.

The FSF in Practice

The FSF provides a standardized, spreadsheet-based platform for assessing fiscal space. Inputs include: (i) initial conditions (debt levels, output gaps, gross financing needs, and contingent liabilities among others); (ii) debt sustainability analysis (from the SRDSF); and (iii) simulations of alternative policy scenarios using macro-fiscal models developed by the Research Department. A detailed assessment table is prepared for internal Fund discussion not is not published in staff reports. Instead, reports for the 69 participating countries provide only a bottom-line assessment, ranging from "no space" to "substantial space." Country teams are encouraged to supplement the tool with judgment, especially where fiscal rules or unmodeled risks are important. The FSF does not generate a numerical estimate of fiscal space or recommend whether space should be used—these are left to staff discretion (IMF, 2022). Teams also decide whether to share the full assessment with national authorities.

Remaining Challenges

While the FSF has enhanced transparency and country tailoring, concerns persist. For example, Clift (2024) argues that in practice Fund policy advice has remained relatively unsupportive of relaxing fiscal policy, at least partly reflecting the inbuilt biases of the analytical frameworks that are used for assessing fiscal space, as well as inbuilt institutional aversion to accepting risks to macroeconomic stability. Other authors (Salamaliki and Venetis, 2024), while not directly criticizing the Fund's approach, argue that nonlinearities—i.e., risks become increasingly severe as thresholds are approached—need to be better accounted for. Many authors have noted that fiscal space assessments have limited relevance for LICs since the risk of losing market access for their debt is less important (Pick, 2017). Lastly, some have questioned whether the focus on numerical methodologies for assessing whether fiscal space exists may distract attention from the reforms that may be needed to existing budgeting frameworks or to expenditure and tax systems (Kentikelenis and Stibbs, 2024).

Interviews of Fund staff and others also surfaced similar concerns. Some staff expressed concern that the tool relied on overly complex debt sustainability analyses, and it also led to an overemphasis on a single metric rather than providing more granular fiscal policy advice. Questions were also raised about whether the review process was sufficient to ensure that the tool was consistently applied. And some interviewees noted that the approach was based on very long-run debt sustainability analyses and led to overly restrictive advice to LICs whose needs were much more immediate. For example, identified shortfalls in fiscal space led to Fund calls for restrictive policies rather than suggestions for how to durably increase fiscal space.

Source: "Fiscal Space Assessment: A Reference Note for Country Teams," February 2023.

Box 2. Debt, Interest, and Growth: How the IMF's Thinking Has Evolved

This box reviews the evolution of IMF views on the relationship between public debt, interest rates, and growth.

Early Views

Early IMF analyses emphasized how higher public debt raises borrowing costs. The November 2009 FM estimated that a 10 percentage point (p.p.) increase in debt raised long-term interest rates by around 50 basis points. Deficits were seen as having a stronger impact, with a 1 percentage point of GDP increase in the deficit pushing up bond yields by 20–60 basis points (Baldacci and Kumar, 2010). Countries with weak fiscal fundamentals or high initial debt (above ~80 percent of GDP) faced even steeper increases. Based on these results, the FM estimated that a persistent increase in debt of about 20 percent of GDP would raise debt service costs by more than 1½ percent of GDP in G-20 countries.

The IMF also endorsed the view that high debt depresses growth, reinforcing concerns about fiscal sustainability. The April 2010 FM estimated that a 10 p.p. increase in debt reduced annual per capita growth by 0.15–0.2 p.p., with significant negative effects already emerging at "medium-to-high" debt levels (above 30–60 percent of GDP) and becoming nonlinear around 60–90 percent of GDP thresholds (Kumar and Woo, 2010). These findings echoed Cecchetti, Mohanty, and Zampolli (2011) and Reinhart and Rogoff (2010), who argued that growth slows sharply when debt exceeds 90 percent of GDP.

Weakening Links in the Great Recession

As AEs accumulated large amounts of public debt after the GFC, IMF research found that the anticipated surge in interest rates largely failed to materialize (October 2014 FM). While traditional estimates of debt sensitivity were still referenced, the Fund recognized that prolonged low rates, QE, and factors like investor risk appetite and safe haven status had weakened the debt-yield link for AEs (Abbas and others, 2013).

At the same time, IMF research increasingly questioned rigid debt thresholds and the causality of the debt-growth relationship. Pescatori, Sandri, and Simon (2014) found no universal tipping point where debt undermines growth, emphasizing that its impact depends on debt stability and whether fiscal policy supports productive investment. Similarly, Panizza and Presbitero (2014) suggested that low growth often drives higher debt, rather than the reverse. While traditional rules of thumb were still referenced (April 2013 FM), the IMF gradually shifted from fixed debt limits to more context-dependent assessments, considering debt trajectories, economic conditions, and the credibility of medium-term consolidation plans.

The "Low-for-Long" Era

By the mid-2010s, it became evident that interest rates on government debt in many AEs had remained below GDP growth rates ($r < g$) for an extended period, challenging earlier concerns about debt sustainability (Blanchard, 2019). The IMF began emphasizing that when $r - g$ is negative, debt-to-GDP ratios can decline organically through growth rather than requiring fiscal consolidation (Ostry, Ghosh, Espinoza, 2015; FM October 2020). This marked a departure from the 2010 stance that prioritized fiscal consolidation.

However, the IMF remained cautious, warning that "low-for-long is not low forever" (Mauro and Zhou, 2020). By 2023, global inflation had pushed interest rates higher. While borrowing costs have risen, there has been no disorderly spike linked to credit risk. Nonetheless, the IMF's October 2022 and April 2023 FM highlighted growing concerns over rising debt service burdens, particularly for economies with already high debt levels (Adrian, Gaspar, and Gourinchas, 2024).

Source: Authors.

8. **The SRDSF's solvency assessment evaluates whether debt is likely to stabilize over the medium term, how uncertain future debt paths are, and how institutional capacity shapes debt-carrying ability.** The debt fanchart module simulates multiple possible debt trajectories over a five-year horizon and summarizes the resulting distribution to illustrate uncertainty, the balance of risks, and prospects for stabilizing the debt-to-GDP ratio. The module reports three metrics: (i) the probability of debt non-stabilization, signaling that baseline policies

may be insufficient to stabilize debt, (ii) the width of the fanchart, reflecting uncertainty around the baseline and the potential for large projection errors, and (iii) the median level of debt in the final year of the projection period adjusted using an institutions index, which captures how governance affects debt-carrying capacity.[3]

9. **In light of past experience with overly optimistic growth and fiscal forecasts, the SRDSF incorporates binding realism tools.** Initially introduced in 2013 as non-binding diagnostics, these tools now require corrections when projections appear unrealistic. Historical fan charts capture the impact of past shocks to primary balances, interest rates, exchange rates, and stock-flow adjustments. If projected debt ratios fall below the 20th percentile of historical distributions, a forecast optimism test is triggered. When the test confirms unrealistic assumptions about the scale of the fiscal consolidation, the framework penalizes the projection by lowering the probability of debt stabilization, thereby compelling staff to revise assumptions prior to publication. These diagnostics are tailored to country comparators—e.g., commodity versus non-commodity EMMIEs—enhancing relevance and specificity.

10. **The SRDSF represents a significant improvement over the previous MAC DSA in capturing sovereign stress linked to liquidity.** As indicated above, the near-term risk assessment module focuses on predicting sovereign stress events over a one-to two-year horizon. It uses an early warning system that incorporates indicators such as institutional quality, past stress episodes, cyclical position, debt burden, buffers, and global conditions to assess the likelihood of near-term liquidity pressures. The Gross Financing Needs (GFN) module also evaluates whether key lenders—often domestic banks—can meet financing requirements under stress scenarios. In addition, the SRDSF flags optimistic assumptions about new borrowing and financing terms by comparing projected maturity profiles with historical patterns and applying the Laubach rule to test the plausibility of spread assumptions.[4]

11. **At the same time, staff pointed to areas where the treatment of liquidity risks in the SRDSF could be further strengthened.** First, although the 2021 guidance allows teams to incorporate liquid assets, staff noted that the practical use of this option has been limited. Stronger and more systematic integration of cash buffers, contingent financing, and market depth would improve realism and policy relevance, particularly for countries with sizable buffers, where fiscal space may otherwise be understated. Second, staff observed that authorities tend to

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[3] A limitation of current frameworks is that they do not readily support scenario analysis of alternative fiscal paths consistent with specified debt targets. The Public Debt Dynamics Tool (DDT)—developed by the IMF's Institute for Capacity Development (Acosta-Ormaechea and Martinez, 2021)—was designed to bridge this gap by providing a practical platform for Fund teams and country authorities to explore alternative fiscal paths and policy scenarios in a transparent and accessible way. The tool computes fiscal adjustment paths to user-defined debt targets, runs standard and customized stress tests, generates fan charts, and presents results in standardized tables. However, the DDT is not a Board-approved DSA tool and remains primarily used for training and capacity development purposes, with only limited application in surveillance or program work.

[4] The Laubach (2009) rule states that bond spreads increase linearly by about 4 basis points in response to a 1 percentage point increase in the projected debt-to-GDP ratio.

place greater weight on the signals from the solvency modules. This can result in reassuring assessments of fiscal sustainability that underplay rollover and market-access risks, leading authorities to believe they have more scope to borrow and finance long-term priorities than may in fact be the case once liquidity pressures emerge.

12. **To address the specific circumstances of LICs, the Fund and the Bank developed a dedicated debt sustainability framework: the LIC-DSF**. The framework applies primarily to PRGT-eligible countries with access to IDA (International Development Association) resources, including all countries eligible for IDA grants.[5] For these economies, external financing is still largely concessional, and the present value of debt is central to assessing debt vulnerabilities, making the LIC-DSF more suitable than the MAC DSA frameworks (IMF and World Bank 2004; IMF 2018b).[6] Like the SRDSF, the LIC-DSF provides a forward-looking analysis of debt dynamics under baseline and stress scenarios, covering both traditional macro shocks (e.g., to export growth) and shocks tailored to LIC circumstances (e.g., natural disasters, commodity price shocks, contingent liabilities, and market access shocks).

13. **First introduced in 2005 and lastly overhauled in 2018, the framework combines indicative thresholds on debt and debt service with staff judgment to assign external public debt distress ratings** (IMF and World Bank, 2005; 2018). Countries are classified as having "strong," "medium," or "weak" debt-carrying capacity, based on a composite indicator that captures institutional strength, reserves, remittances, domestic and global growth. Since the 2018 Guidance Note, new challenges have grown in importance—including heightened risks from climate change, greater reliance on commercial and domestic borrowing, and a rising number of complex debt restructurings—prompting the need for more tailored implementation guidance. A Supplement to the 2018 Guidance Note, published in 2024 (IMF and World Bank, 2024), provides additional direction on how to address these issues within the current framework.

14. **The 2017 review of the LIC-DSF introduced four realism tools to strengthen the credibility of debt sustainability analyses.** These tools assess (i) the drivers of past and projected debt dynamics; (ii) the magnitude and plausibility of planned fiscal adjustments; (iii) the consistency between projected growth and the assumed pace of fiscal consolidation; and (iv) the coherence between projected growth and public investment paths. Each tool serves as a diagnostic rather than a binding constraint, prompting staff to justify departures from typical

[5] Countries that graduate from PRGT eligibility may still remain within the LIC-DSF framework under certain circumstances. Graduation from the LIC-DSF can be delayed if there are significant short-term vulnerabilities, such as risks of losing market access or high borrowing costs, or if sufficient information is not available to apply the MAC DSA tools. Additionally, operational considerations for IDA financing may necessitate the continued use of the LIC-DSF for some countries, even after they have graduated from PRGT eligibility.

[6] If the discount rate and the contractual interest rate of a loan are the same, then the present value is equal to (or close to) the face value. If, however, the contractual interest rate of the loan is less than the discount rate, then the PV of the debt is less than the face value, implying that the loan has some degree of concessionally (IMF and World Bank, 2013).

experience and to ensure that baseline assumptions are grounded in realistic expectations. Together, these diagnostics encourage more rigorous scrutiny of the macro-fiscal framework by highlighting instances where debt reductions rely on historically uncommon adjustments or implausibly strong growth effects from fiscal or investment plans, thereby improving the transparency and credibility of the LIC-DSF.

15. **While the framework has made progress in capturing liquidity pressures in LICs, its coverage remains incomplete.** The main channel is the Market Financing Pressures Tool, applied to LICs with market access, which checks in the baseline whether gross financing needs and EMBI spreads exceed critical thresholds (14 percent of GDP and 570 basis points, respectively). Country teams may also apply a tailored "market financing" stress test simulating adverse shifts in global risk sentiment, exchange rate depreciation, and shorter maturities on new borrowing. These innovations mark progress in recognizing liquidity risks. At the same time, the growing fragmentation of debt portfolios over the past decade—across bilateral creditors, private investors (especially bondholders), and domestic markets—has heightened the relevance of liquidity risks and underscores the need for more systematic analysis of maturity and currency composition, which are critical for rollover risk. The comprehensive review of the LIC-DSF now underway is expected to strengthen the integration of liquidity considerations.[7]

16. **Finally, despite their analytical richness, insights from DSA tools appear underutilized in Article IV surveillance policy discussions.** While staff noted good integration of DSA outputs in Fund-supported programs, the same cannot always be said for surveillance work. A review of over 200 staff reports from 2008 to 2023 found significant variation in how DSA results were reflected in the main policy discussion, including for counties where fiscal sustainability was a relevant issue (Cohen-Setton and Montiel, 2025; Zoli and Ocampo, 2025; De Lannoy and Lane, 2025). In some cases, DSAs were relegated to appendices without influencing the fiscal advice; in others, key findings were referenced without a clear link to policy recommendations. More systematic use of DSA insights could enhance the credibility and operational relevance of fiscal advice, especially as countries confront tightening financing conditions and rising medium-term spending needs.

Fiscal Space Assessment and Analysis of Fiscal Risks

17. **The Fund introduced the Fiscal Space Framework (FSF) in 2016 to assess whether countries could expand fiscal policy without jeopardizing market access or debt sustainability.** Defined as "the room to raise spending or lower taxes relative to a pre-existing baseline, without endangering market access and debt sustainability" (IMF, 2018a), the concept of fiscal space was conceived as a guide for countercyclical policy during downturns and for supporting socially productive public investment. It has informed both bilateral surveillance and multilateral guidance, with the April 2017 FM featuring country-specific estimates of available

[7] Since 2024, the LIC-DSF has incorporated domestic debt service indicators to better capture rollover risks (IMF and World Bank, 2024).

fiscal space. While the concept of fiscal space has long featured in Fund advice, the introduction of a formal tool marked a step forward in systematizing assessments. Since 2018, fiscal space assessments have been required for 69 countries—including 41 EMMIEs and 5 LICs with market access—though these requirements were temporarily suspended during the COVID-19 Pandemic (2020–early 2023).

18. **Yet the framework's influence in practice remains contested.** A desk review of Article IV reports for advanced economies by Cohen-Setton and Montiel (2025) found that fiscal space assessments in recent years were more convincing and differentiated than in the early part of the 2008–23 evaluation period, a development they attribute to the introduction of the FSF, which helped standardize assessments and reduce reliance on judgment. At the same time, external critics argue that Fund advice has remained overly cautious in recommending fiscal expansion, even after the FSF's adoption. Some staff also voiced concern that reliance on a single composite indicator has crowded out more granular analysis and constrained the flexibility needed to adapt advice to country-specific contexts. These limitations underscore the need for greater clarity on how FSF diagnostics should be interpreted and how they should be integrated with broader macro-fiscal considerations, including political economy constraints and long-term spending needs (for more on the FSF, see Box 1).

19. **Recent crises have underscored that unmanaged fiscal risks can upend macroeconomic plans and debt paths.** The GFC, commodity-price collapses, the pandemic, and climate-related shocks revealed large downside, correlated realizations of risk that propagate through public balance sheets. Historically, governments have faced an adverse fiscal shock averaging about 6 percent of GDP roughly once every twelve years (IMF, 2016c). These episodes highlighted gaps in transparency, coverage of the broader public sector, and the need to quantify how macro shocks and contingent liabilities interact to threaten solvency, liquidity, and financing capacity.

20. **Against this backdrop, the IMF expanded its fiscal-risk work along two complementary tracks: (i) standards and diagnostics to embed risk identification, disclosure, and governance in country systems; and (ii) a modular toolkit to quantify exposures and transmission channels and to inform buffers, fiscal rules, and DSA scenarios.** On the first track, a revamped Fiscal Transparency Code introduced a dedicated Pillar III on "Fiscal Risks," now accounting for roughly one-third of the assessment, operationalized through Fiscal Transparency Evaluations that have informed surveillance and program design. On the second track, an initial Board paper on best practices (IMF, 2016c) catalyzed the development of a comprehensive Fiscal Risk Toolkit (Figure 1) that countries and area departments can apply at different capacity levels and link to LIC and MAC DSAs, MTDS, and calibration of fiscal anchors.

Figure 1. Fiscal Risk Toolkit

Source: IMF.

21. **The Fund's systemwide tools broaden coverage beyond deficits and debt to the full public sector and to tail risks.** The Public Sector Balance Sheet (PSBS) work (October 2018 Fiscal Monitor) produced a cross-country PSBS database (Alves, De Clerk, and Gamboa-Arbelaez, 2020) that consolidates assets and liabilities—including SOEs, natural resources, and pensions—and supports balance-sheet risk assessments and fiscal stress tests. The Fiscal Stress Test (FST) integrates macro shocks with contingent-liability realizations to quantify impacts on solvency (comprehensive net worth), liquidity (gross financing needs), and financing burden (interest-to-revenue), and to derive stress scenarios for DSA and buffer sizing. The Fiscal Risk Assessment Tool (FRAT) provides a portfolio view across fourteen risk categories, prioritizes monitoring/mitigation, and links to transparency assessments. More recently, the Debt-at-Risk framework (October 2024 Fiscal Monitor; Furceri and others, 2025) applies a quantile-regression approach to map macro-financial and political conditions to the distribution of future debt outcomes; while outside our sample window, it illustrates continuing methodological upgrades.

22. **Risk-specific modules deepen analysis where exposures are large.** For public corporations, the SOE Health Check Tool screens vulnerabilities and aggregates sector balance sheets, while the SOE Stress Test projects cash flows, liquidity, and debt-servicing resilience under baseline and stress scenarios—informing budget contingencies and DSA shocks. For credit support, the Discrete Guarantees and Loans Assessment Tool (DGLAT) estimates expected fiscal costs and maximum exposures on entity-specific loans and guarantees, and the Standardized Guarantees Assessment Tool (SGAT) values scheme-level portfolios under baseline and stress cases to inform pricing, provisioning, and disclosure. For infrastructure, the PPP Fiscal Risk Assessment Model (PFRAM, with the World Bank) quantifies cash- and accrual-basis impacts, sensitivity, and risk allocation at the project/portfolio level. For climate, Q-CRAFT projects long-horizon macro-fiscal paths under alternative IPCC scenarios (and adaptation speeds), supporting integration of climate risks into fiscal frameworks and fiscal risk statements.

23. **The Fund's work on fiscal risks has established an impressive and comprehensive analytical architecture, but its application has remained incomplete.** Building on lessons from past crises, the IMF has developed a wide-ranging set of standards, databases, and tools that allow countries to identify, quantify, disclose, and manage fiscal risks, as well as to integrate stress scenarios into surveillance and program design. These innovations—spanning fiscal transparency evaluations, public sector balance sheet analysis, and a suite of specialized tools—represent a major step forward in how fiscal vulnerabilities are conceptualized and operationalized across the membership. Yet, implementation has been uneven: efforts to build a cross-country dataset on contingent liabilities (Bova and others, 2016) were not sustained, leaving significant gaps in the empirical foundation for fiscal risk assessments, and the systematic use of these tools in bilateral surveillance has remained limited. Strengthening the consistency of application across countries, particularly where climate, SOE, and financial-sector linkages are macro-critical, and renewing cross-country data collection would substantially enhance their policy impact.

III. OUTPUT STABILIZATION

24. **The Global Financial Crisis (GFC) prompted a fundamental reassessment of the role of discretionary fiscal policy at the IMF.** In September 2008, newly appointed Chief Economic Counsellor Olivier Blanchard prioritized a rethink of fiscal activism in light of the sharp collapse in global demand. A pivotal moment in this intellectual shift—widely recognized in the literature (Ban, 2015) and in staff interviews—was the December 2008 Staff Position Note *Fiscal Policy for the Crisis*, co-authored by Spilimbergo, Symansky, Blanchard, and then-FAD Director Cottarelli. The paper challenged pre-crisis orthodoxy by outlining principles for effective stimulus—arguing it should be timely, large, lasting, diversified, contingent, collective, and sustainable. This work was complemented by a practical manual (Spilimbergo, Symansky, and Schindler, 2009) to help IMF desk economists incorporate fiscal considerations into macroeconomic frameworks. Staff interviews suggest the episode was as much about building internal consensus as introducing new ideas and was underpinned by new empirical work on fiscal multipliers and spillovers.

Fiscal Policy Effects

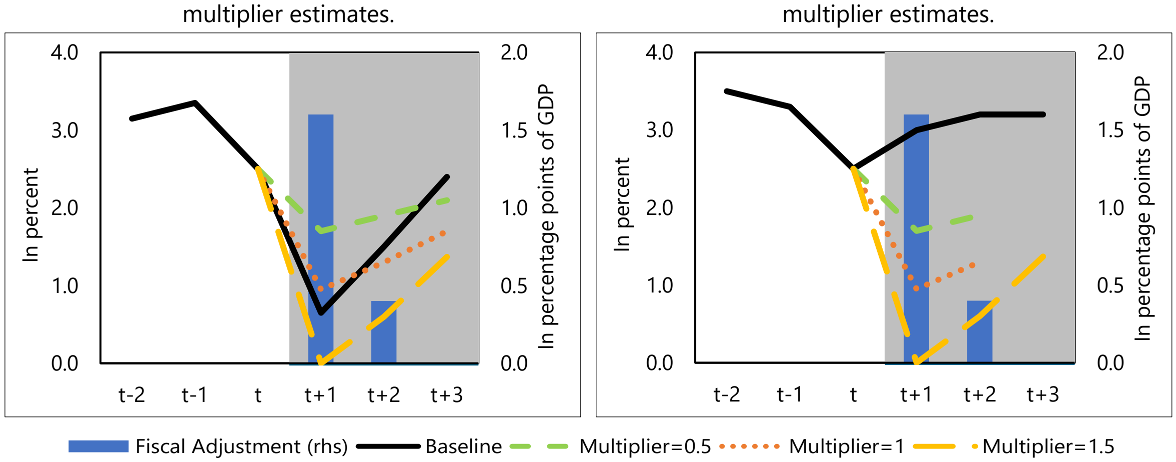
25. **IMF research played a central role in dismantling the "expansionary fiscal contraction" hypothesis and documenting the output costs of consolidation.** While earlier work had shown some ambivalence toward the idea of expansionary austerity (Daniel and others, 2006), post-crisis research provided robust evidence that consolidations are generally contractionary. The October 2010 WEO chapter *Will It Hurt?* introduced the narrative method developed by Romer and Romer (2010) to isolate exogenous episodes of fiscal consolidations. The resulting dataset, later published by Devries and others (2011), became a benchmark for studying the effects of consolidation on output, employment, external balances, and inequality (Ball and others, 2013; Woo and others, 2013). Initially focused on 17 OECD countries over 1978–2009, the dataset has since been expanded to include EMMIEs and cover more recent periods (Carrière-Swallow, David, and Leigh, 2018; Adler and others, 2024), cementing its role in IMF surveillance and research.

26. **These findings, and evidence that staff systematically underestimated fiscal multipliers (Blanchard and Leigh, 2013), led to the development of the Fiscal Multiplier Realism Tool in the revamped DSA framework.** The tool assesses whether growth projections are consistent with the size and timing of planned fiscal adjustments (IMF, 2021b; 2022b). As shown in Figure 2, the tool compares baseline growth forecasts with those implied by a range of plausible multipliers (0.5–1.5). In the left panel, no realism flag is raised, as the baseline projection falls within the expected range given reasonable multipliers. In contrast, the right panel flags a potential issue, as it assumes growth will accelerate despite large fiscal tightening, suggesting overly optimistic assumptions.

Figure 2. Fiscal Multiplier Realism Tool in the SRDSF
(Fiscal Adjustment and Possible Growth Paths)

A. No Realism Issues
Growth weakens while a large fiscal adjustment is undertaken, consistent with reasonable multiplier estimates.

B. Realism Issues
Growth remains high while a large fiscal adjustment is undertaken, inconsistent with reasonable multiplier estimates.



Source: IMF (2022b).
Note: A similar fiscal multiplier realism tool is incorporated in the LIC-DSF for PRGT-eligible countries, with the range of plausible multipliers set between 0.2 and 0.8.

27. **Despite these analytical advances, empirical work often falls short in providing the methodological detail necessary for rigorous scrutiny and replication.** While most studies include technical documentation, key assumptions are not always specified clearly enough to permit independent validation, which limits external scrutiny and undermines confidence in the robustness of findings. For instance, studies using instrumental-variable approaches often provide insufficient information to assess the strength and relevance of the instruments, while papers employing sign restrictions do not always disclose the exact restrictions applied. This concern is especially salient for macro-fiscal studies—such as those estimating state-dependent fiscal multipliers—which tend to be highly sensitive to model specification, country context, and identification strategy. To enhance transparency and practical usefulness, fewer but more clearly presented results, accompanied by full methodological documentation, would be preferable. Main texts should explicitly identify the preferred model or set of estimates and briefly explain

why they were chosen over alternatives, while annexes should be self-contained, linking each key result in the text to the underlying data, model structure, assumptions, and estimation methods. Finally, the publication of replication packages—especially for flagship studies—would significantly strengthen the credibility, replicability, and policy relevance of the Fund's empirical work.[8]

28. **The multiplier literature remains heavily AE-focused, with limited country-specific guidance for EMDEs.** Interviewees noted that the Fund often relies on stylized cross-country estimates and that staff rarely discuss instrument-specific multipliers in depth—particularly in countries with data constraints or limited analytical capacity. Some empirical work does exist: the October 2008 WEO provided early estimates for EMMIEs,[9] followed by surveys of the literature such as Batini and others (2014) and regional analyses including González-García and others (2013) for the Eastern Caribbean Currency Union. More recent Regional Economic Outlooks have extended the evidence to Latin America (Carrière-Swallow, David, and Leigh, 2018; October 2020 Western Hemisphere REO) and Sub-Saharan Africa (October 2017 Sub-Saharan Africa REO), while studies such as Honda, Miyamoto, and Taniguchi (2020) and Geli and Moura (2023) broadened coverage across income groups. Still, significant gaps remain, with limited country-specific analysis and little systematic evidence outside a few regions.[10]

29. **Beyond discretionary policy, the IMF has emphasized the importance of well-designed automatic stabilizers.** The Spring 2015 FM found that in 60 percent of AEs, automatic stabilizers accounted for over half of total fiscal stabilization. However, their underuse in expansions often led to asymmetry in fiscal responses and contributed to debt accumulation. For EMMIEs, the contribution of automatic stabilizers was estimated at just 30 percent. The IMF (2020) also explored stabilizers in Latin America, identifying legal and institutional reforms—such as embedding cyclical tax adjustments, indexing transfers, or pre-legislating stimulus triggers—as key to improving their effectiveness. Building on earlier work (Baunsgaard and Symansky, 2009), the Fund argued that strengthening automatic stabilizers could improve both the timeliness and reversibility of fiscal responses, reducing reliance on discretionary measures that are often delayed and politically contentious. The October 2022 FM compared the costs of discretionary policies versus automatic stabilizers policies and their impact on consumption and employment.

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[8] Similar observations and recommendations were made by an external panel report on FAD policy analysis (Ramey, Ball, Giavazzi, 2024).

[9] The earlier IMF Staff Position Note (Spilimbergo, Symansky, and Schindler, 2009) provided little specific evidence for EMMIEs.

[10] An ongoing project led by the Research Department estimates fiscal multipliers using an array of different methodologies, including AI tools for better identification of "fiscal shocks." The multiplier estimates as well as the underlying data and codes will be made available to the country teams to allow them to tailor estimates further to their countries.

Fiscal Spillovers

30. **The IMF has incorporated the analysis of fiscal spillovers into its surveillance work, recognizing that the cross-border effects of national fiscal policies can be substantial.** Between 2011 and 2013, dedicated *Spillover Reports* assessed the external effects of domestic policies in five systemic economies—China, the euro area, Japan, the United Kingdom, and the United States—drawing on background analytical work. From 2014 to 2015, these reports adopted a more thematic focus, addressing spillover issues of global concern. Since 2016, spillover analysis has been integrated into the WEO, with an annual chapter devoted to global transmission channels. A notable example is Chapter 4 of the October 2017 WEO, *Cross-Border Impacts of Fiscal Policy: Still Relevant?*, which used Structural Vector Autoregressions (SVARs), the G-20 general equilibrium model, and a narrative identification approach to estimate fiscal spillovers. The analysis found that spillovers are larger when domestic fiscal multipliers are high, government spending (rather than revenue) drives the adjustment, and exchange rates are fixed—highlighting the conditions under which fiscal policy has the greatest international impact.[11]

31. **The Fund has also developed a suite of global macroeconomic models to quantify fiscal spillovers and support cross-country policy analysis.** The Global Integrated Monetary and Fiscal Model (GIMF), a dynamic general equilibrium model featuring multiple regions and rich fiscal structure, has been widely used to evaluate fiscal policy in both advanced and emerging economies (Kumhof and Laxton, 2007; Kumhof and others, 2010). To complement GIMF and support more flexible, large-scale simulations—particularly in the G-20 context—the Fund developed the Flexible System of Global Models (FSGM) (Andrle and others, 2015). These tools allow staff to analyze the global implications of coordinated or asymmetric fiscal actions and assess how fiscal policy decisions in one country may amplify or dampen external imbalances, inflation, or financial stability risks elsewhere.

Trade-offs and Debt Anchors

32. **The IMF has increasingly recognized the inherent trade-off between output stabilization and fiscal sustainability.** Stimulus may be necessary to close negative output gaps—particularly when monetary policy is constrained—but it can strain public finances by increasing borrowing needs or heightening rollover risks. Conversely, fiscal consolidation undertaken to improve debt dynamics may depress output in the short term, especially when implemented during periods of economic slack. These tensions underscore the importance of the timing, composition, and credibility of fiscal measures in minimizing short-term costs while safeguarding long-term sustainability. The experience of the global financial crisis and the COVID-19 pandemic has highlighted how difficult it can be to strike this balance in real time:

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[11] At the bilateral level, Article IV consultations frequently assess inward spillovers, analyzing how external shocks affect a country's economy. Recent staff reports on systemic economies (Systemic Five)—the U.S., China, the euro area, Japan, and the U.K.—have expanded coverage of outward spillovers, evaluating how their policies impact the global economy. The 2018 U.S. Article IV staff report, for instance, examined outward spillovers from the 2017 Tax Cuts and Jobs Act.

decisive fiscal support helped cushion activity but left many countries with sharply higher debt burdens, complicating subsequent policy choices. Against this backdrop, the IMF has placed growing emphasis on developing analytical frameworks that can guide policymakers in navigating these trade-offs more systematically, while recognizing that country circumstances and market perceptions inevitably shape the policy space available.

33. **To navigate the trade-off between supporting activity and safeguarding fiscal sustainability, the IMF developed a toolkit to quantify the optimal pace of fiscal adjustment.** Traditional DSAs and FSF assessments indicate how much additional debt can be incurred without endangering sustainability, or how much needs to be reduced to restore it.[12] But they do not address whether it is desirable to expand or contract debt under prevailing macroeconomic conditions, nor the appropriate speed of adjustment. A model developed by FAD economists (Fournier, 2019; Fournier and Lieberknecht, 2020) fills this gap by providing an optimizing framework in which governments balance the short-term benefits of countercyclical fiscal support against the long-term costs of higher debt. When debt is low, the model permits more forceful stimulus in downturns; when debt is high, it recommends greater caution to preserve buffers and market confidence. The tool has been used in surveillance for AEs, with the European Department deploying an automated dashboard to generate country-specific fiscal paths. An extended version of the model that accounts for a portion of public debt to be denominated in foreign currency has also been developed and applied to EMDEs, including Mexico (Fournier and Roemer, forthcoming).

34. **While the optimizing framework provides useful guidance on the *pace* of adjustment, it does not resolve the equally important question of the *appropriate anchor* for medium-term fiscal policy.** Earlier efforts, such as Eyraud and others (2018) and Akitoby, Honda, and Miyamoto (2019), developed a structured methodology for calibrating medium-term debt anchors based on debt-servicing capacity and safety buffers, and these tools have been applied widely in Fund surveillance and capacity-development work.[13] Yet, these approaches concentrate on fiscal sustainability rather than on balancing different objectives, and thus offer only a partial basis for policy advice. Moreover, IEO reviews of staff reports show that medium-term debt targets in both surveillance (Cohen-Setton and Montiel, 2025) and programs (Cohen-Setton, Li, and Montiel, 2024) often vary across countries and over time without clear justification. This raises questions both about whether alternative adjustment paths and debt targets might have offered better policy trade-offs and about whether long-term considerations have been incorporated consistently and evenhandedly across countries facing similar circumstances.

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[12] An FAD toolkit based on Cao and others (forthcoming) offers operational guidance to calibrate country-specific maximum sustainable debt and complements earlier work by Caselli and others (2022).

[13] IMF (2018b, 2023) proposed a three-step methodology: first, estimating a medium-term debt limit based on countries' debt repayment capacity; second, calibrating a safety buffer around that limit using historical macroeconomic and fiscal volatility; and third, deriving the debt anchor as the difference between the debt limit and the buffer. This approach provides a transparent template for assessing prudent debt levels, but it is anchored in debt-servicing capacity rather than in considerations of expenditure needs or development priorities. Comelli and others (2023) apply that approach to Sub-Saharan countries.

35. **A constructive way forward would be to make the rationale for selecting one option from the feasible set of medium-term debt targets more explicit**. One approach would be to adopt a common template for evaluating alternative medium-term debt targets, based on defined set of costs and benefits—not only in terms of fiscal sustainability and debt-servicing capacity, but also in relation to financing priority expenditures that could be applied across member countries.[14]

IV. POTENTIAL OUTPUT AND OTHER LONGER-TERM ISSUES

36. **In response to slowing growth after the GFC, the Fund deepened its analytical work on how fiscal policy could foster investment, productivity, and long-term growth.** The October 2014 WEO chapter highlighted the case for higher public investment in AEs, particularly against the backdrop of low interest rates and concerns about secular stagnation (Cohen-Setton and Montiel, 2025). For EMMIEs, it found that while public investment can boost long-term output, it often raises debt-to-GDP ratios due to lower investment efficiency—underscoring the need to strengthen efficiency to mitigate this trade-off. In parallel, the Debt, Investment, Growth, and Natural Resources (DIGNAR) model was developed to assess the macroeconomic impact of public investment plans in resource-rich developing economies (Melina, Yang, and Zanna, 2014). Building on this work, the October 2025 FM analyzed how the efficiency of different categories of government spending shapes their long-term growth impact.

37. **To support countries in achieving the SDGs, the IMF has developed methodologies to estimate additional spending needs and assess financing options.** The spending needs framework benchmarks countries against well-performing peers to identify investment gaps in human capital (health and education) and physical infrastructure (water, sanitation, electricity, and roads) (Gaspar and others, 2019; Carapella and others, 2023). Building on this work, the IMF (2024) developed the SDG Financing Tool (SDG-FiT), an interactive platform that allows users to test alternative financing strategies, evaluate their macroeconomic consistency, and compare policy options. Together, these tools are designed to strengthen long-term development planning by clarifying the fiscal implications of pursuing SDG-related objectives.

38. **The Fund has also highlighted that the effectiveness of structural reforms depends on the degree of policy support.** Two WEO chapters—focusing respectively on AEs and on EMMIEs and LICs—showed that labor market deregulation delivers larger output gains when implemented under favorable economic conditions and complemented by supportive fiscal measures (IMF, 2016b, 2019b; Duval, Furceri, and Jalles, 2019; Duval and Loungani, 2019). These findings underscore the importance of sequencing and coordination between structural and macro-fiscal policies.

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[14] An extension of the buffer-stock model goes in the direction of deriving debt anchors endogenously, with the expected debt path emerging as an outcome of the optimization process between fiscal sustainability and output stabilization, conditional on assumptions about time preference, the size of shocks, and the debt carrying capacity, potentially calibrated to reflect a given tolerance for debt risks (Fournier and Roemer, forthcoming).

39. **Building on this focus of policy complementarities, the IMF also emphasized the synergies among fiscal, monetary, and structural policies in the context of declining interest rates.** Analytical work—including the April 2016 WEO, the October 2014 FM, and a Staff Discussion Note by Gaspar, Obstfeld, and Sahay (2016)—showed how well-targeted fiscal measures, such as investment in education and childcare or cuts in labor taxes, could support growth at different horizons while facilitating monetary policy normalization. Such measures broaden the tax base, strengthen fiscal sustainability, and raise potential output. By lifting the natural rate of interest, they also expand the room for monetary policy, reinforcing a virtuous cycle of macroeconomic stability. At the same time, staff interviews revealed tensions around this agenda: central bank governors in Europe pushed back against the so-called "3C paper" by Gaspar, Obstfeld, and Sahay (2016), which called for a Comprehensive, Consistent, and Coordinated approach and advocated a more active role for fiscal policy. Governors stressed that monetary autonomy required fiscal restraint, warning that loose fiscal policy could undermine efforts to control inflation and maintain credibility. Staff acknowledged these concerns but countered that prolonged subpar growth carried its own perils.

40. **The Fund has strengthened its analysis of fiscal policy as a tool for inclusive growth.** A growing body of IMF research (Box 3) shows that redistribution can enhance both equity and growth, challenging the traditional view of a trade-off. The October 2017 FM discussed fiscal measures to support redistributive goals, while Furceri and others (2021) demonstrated that deeper post-pandemic fiscal consolidations have historically been associated with larger increases in inequality. To support operational advice, FAD has developed the Social Protection and Labor Assessment Tool (SPLAT), which benchmarks countries' social protection systems against peers and helps tailor recommendations, e.g., expanding coverage, improving targeting, and adjusting benefit adequacy. More recently, the October 2024 FM and October 2025 FM analyzed the growth and distributional impact of public spending and investment.

41. **The IMF has developed a suite of datasets and tools to support fiscal policy analysis related to climate change, though concerns have been raised about their resource implications.** Three working papers (Coady and others, 2019; Parry, Black, and Vernon, 2021; Black and others, 2023a) produced detailed estimates of global fossil fuel subsidies. In 2021, the Fund launched the Climate Change Indicators Dashboard to provide a platform for climate change data for macroeconomic and financial stability analysis. In collaboration with the World Bank, the Fund created the Climate Policy Assessment Tool (CPAT) to estimate the fiscal, environmental, and economic effects of carbon pricing, fossil fuel subsidy reform, and green investment packages (Black and others, 2022; 2023b). A joint FAD–Asia and Pacific Department study (IMF, 2021c) evaluated the growth-debt trade-offs of adaptation and mitigation strategies in emerging markets, while a DSGE model calibrated for small developing states assessed the macroeconomic returns to adaptation investment (Fernandez-Corugedo, Gonzalez-Gomez, and Guerson, 2023). The Quantitative Climate Change Risk Assessment Fiscal Tool (Q-CRAFT) was added to the Fiscal Risk Toolkit to assess long term fiscal risks from climate change. Despite these advances, several interviewees raised concerns that the proliferation of climate-related

initiatives across departments has diverted resources from other core areas of Fund work which, in their view, could have undermined traction and operational relevance in more traditional areas of fiscal surveillance.

Box 3. The IMF's Growing Focus on Income Distribution in Fiscal Advice

The IMF's approach to income distribution has undergone a significant transformation over the past several decades, shifting from a peripheral concern to a central element of its policy advice. Initially, the IMF focused primarily on macroeconomic stability, growth, and fiscal sustainability, paying little attention to inequality. By the late 1980s and 1990s, however, concerns about the economic and political sustainability of adjustment programs led the Fund to integrate social safety nets into its lending programs (Clements, Gupta, and Nozaki, 2013) and emphasizing the need to safeguard social spending on health and education during fiscal adjustments (Gupta and others, 2000). Yet, at this stage, income distribution was still seen largely as a secondary issue, rather than a macro-critical factor affecting growth and stability. The GFC of 2008–09 marked a turning point in the IMF's perspective on inequality, as the crisis exacerbated income disparities and intensified global debates about income and wealth distribution.

The IMF's Research Department (RES) began producing influential studies that challenged traditional economic assumptions. Berg and Ostry (2011) demonstrated that higher inequality is associated with shorter and less durable growth spells, suggesting that inequality is not just a social issue but a key determinant of macroeconomic performance. Subsequent research by Ostry, Berg, and Tsangarides (2014) found that redistributive policies do not necessarily harm growth, contradicting the view that redistribution always weakens economic efficiency. These findings—reinforced by Dabla-Norris and others (2015), who showed that income growth among the bottom 20 percent of earners is associated with stronger GDP growth—helped shift the IMF's perspective, elevating inequality from a secondary outcome of economic policies to a core policy concern in its own right. According to Clements and others (2015), a key lesson from this research is that well-designed tax and spending measures can simultaneously foster stronger economic growth and enhance equality. Senior IMF staff emphasized in interviews that this shift reflected a broader evolution in the economics profession, which increasingly recognized the unequal effects of policies. They highlighted the influential findings of Autor, Dorn, and Hanson (2013) on the unequal effects of trade policies, noting that similar distributional considerations had also become central to fiscal policy discussions. They also explained that inequality pilots were launched in 2015-17. Later, working with the U.K.'s DFID, general equilibrium models were developed.

By the mid-2010s, the IMF had integrated income distribution concerns into its flagship publications, **including the WEO and FM.** The 2014 FM emphasized that fiscal policy is a powerful tool for reducing inequality, advocating for more progressive tax policies, better-targeted social transfers, and stronger investment in human capital. Similarly, the 2017 FM devoted an entire chapter to examining how governments could use tax and spending policies to mitigate inequality without undermining growth. These analyses reflected the Fund's growing recognition that excessive inequality can erode social cohesion, weaken demand, and ultimately threaten financial stability. As part of this shift, the IMF increasingly cautioned AEs to avoid austerity measures that disproportionately harm lower-income groups and to implement more progressive tax structures, including higher taxes on wealth and property (Bastagli, Coady, and Gupta, 2012).

The evolution of the IMF's stance was also shaped by institutional and leadership changes. Under Christine Lagarde's tenure as Managing Director (2011–19), the Fund placed a stronger emphasis on inclusive growth and social protection. Lagarde frequently underscored the risks of rising inequality, warning that it could undermine long-term economic stability and social cohesion (Lagarde, 2013). This shift was reflected in the 2019 IMF social spending strategy, which formally committed the Fund to integrating social protection considerations into its policy advice and technical assistance (IMF, 2019a). The strategy encouraged governments to preserve or expand social spending, even in the context of fiscal consolidation, and to design tax policies that ensure a fairer distribution of the adjustment burden (Clements and others, 2015). By this point, the IMF's position had moved beyond simply acknowledging inequality to actively promoting policies that reduce it. The IMF's evolution has continued into the 2020s, particularly in response to the COVID-19 pandemic. Under Kristalina Georgieva's leadership, the Fund has emphasized that fiscal policies should support a more equitable recovery, including through targeted social transfers, expanded healthcare and education spending, and progressive taxation (October 2020 FM).

Source: Clements and others (2015).

42. **Staff in area departments noted that several tools designed to address longer-term challenges—such as DIGNAR, SPLAT, CPAT, GMMET, and SDG-FiT—tend to be treated as "add-ons" rather than integrated into core surveillance products.** In particular, their outputs are often developed in parallel to, rather than embedded within, the debt sustainability framework. This limits their influence on policy discussions and weakens the coherence between long-term scenario analysis and short- to medium-term fiscal advice. Staff suggested that a more systematic incorporation of long-term scenarios into DSAs and baseline projections—similar to the approach adopted for climate considerations in the LIC-DSF—would enhance the operational relevance of these tools and ensure greater consistency across country work.

V. ASSESSMENT

43. **While the IMF's fiscal policy advice has traditionally emphasized fiscal sustainability, the institution has demonstrated notable agility in adapting to shifting macroeconomic realities**. As economic conditions evolved, the Fund broadened its approach to recognize the central role of fiscal policy in demand management, especially during periods of subdued growth and constrained monetary policy. This evolution was underpinned by a strong commitment to research-driven policymaking, fostering an environment in which established ideas are continually reassessed and analytical resources redirected toward areas with greatest potential payoffs. The Fund's analytical work has evolved in step with advances in the economics profession, at times positioning the institution as an intellectual leader. As a result, it has played an active role in shaping global policy debates—offering evidence-based insights on fiscal consolidation, the implications of low interest rates for fiscal sustainability, the macroeconomic effects of climate transition policies, and the distributional consequences of fiscal measures.

44. **The Fund has also made significant progress in developing analytical toolkits that enhance the rigor, consistency, and transparency of its fiscal advice.** The FSF and SRDSF represent important advances, providing structured frameworks to assess countries' debt-carrying capacity while accounting for institutional quality, financing conditions, and the interest–growth differential. Normative tools developed by FAD further quantify trade-offs between output stabilization and debt sustainability, informing advice on fiscal adjustment paths and policy sequencing. Complementary realism tools—such as the Fiscal Adjustment and Fiscal Multiplier Realism Tools embedded in the SRDSF—have reduced the risk of overly optimistic forecasts by grounding projections in empirical evidence and historical experience.

45. **Despite important advances, key limitations remain—both in the transparency of empirical analysis and the coverage of critical policy questions** Some studies lack sufficient documentation to allow for replication or rigorous scrutiny, making it difficult to assess the robustness of their findings. Moreover, much of the empirical analysis remains concentrated on AEs, with less coverage of EMDEs, where fiscal transmission mechanisms and policy trade-offs differ markedly. Expanding the empirical base and improving methodological transparency would strengthen the credibility and policy relevance of the Fund's analytical work. Expanding the empirical base and improving methodological transparency would strengthen the credibility

and operational relevance of the Fund's analytical work. In addition, several dimensions of fiscal policy analysis remain underdeveloped—including the articulation of the fiscal–monetary policy mix,[15] the integration of long-term policy goals into sustainability assessments, the identification of desirable medium-term debt targets, and the treatment of distributional and political economy factors. The following paragraphs discuss these gaps in greater detail.

46. **A clearer analytical framework is also needed to guide advice on the appropriate fiscal–monetary policy mix for short-term stabilization outside of ZLB episodes.** Such assessments depend not only on the size of fiscal multipliers but also on the effectiveness of monetary transmission. While this issue was less salient in the post-GFC period, given the ZLB in many advanced economies or the lack of monetary autonomy in euro area countries, it is increasingly relevant elsewhere. To ensure fiscal policy plays an effective stabilizing role under varying monetary conditions, staff would benefit from objective guidance to assess how country-specific factors influence the strength of monetary transmission and, in turn, the optimal policy mix.

47. **Beyond short-term stabilization, the integration of fiscal sustainability analysis with long-term policy objectives remains incomplete.** IMF staff have produced valuable work on the macroeconomic effects of fiscal policies aimed at advancing longer-term goals such as improving the quality of public infrastructure, strengthening defense capabilities, promoting redistribution, and supporting climate adaptation. However, the feedback effects of these measures on fiscal sustainability, including their impact on growth, revenues, and permanent spending, are rarely quantified. More systematic assessment of these effects would help determine the extent to which such policies ultimately strengthen or weaken the public sector's balance sheet. Ultimately, the implications of these policies depend not only their social returns but also on the fiscal returns accruing to the state.

48. **Similarly, while existing frameworks assess whether public debt trajectories are sustainable and feasible, they offer little guidance on how to choose among alternative fiscal paths anchored by different medium-term debt targets.** The SRDSF, LIC-DSF, and FSF provide valuable assessments of sustainability, while FAD's optimization tool quantifies the trade-off between output stabilization and fiscal consolidation. Yet, the rationale for selecting a specific terminal debt target—say, converging to 60 rather than 65 percent of GDP—remains largely judgment-based and focused narrowly on fiscal sustainability. A more systematic approach that explicitly articulates the trade-offs among fiscal objectives—such as sustainability and the financing of priority investments—would help determine which medium-term debt paths are most desirable given country circumstances and policy priorities.

[15] The evaluation did not identify dedicated IMF toolkits assessing the appropriate fiscal–monetary policy mix outside of the ZLB. This gap is therefore discussed only in the assessment rather than in the main text.

49. **A more complete understanding of fiscal sustainability also requires deeper analysis of the distributional effects of fiscal policy.** Building on influential research from the 2010s and the 2019 Social Spending Strategy, Fund departments have analyzed the distributional impact of fiscal policy changes, with a justified focus on protecting the poorest. To enhance the policy relevance of this work, future efforts should extend beyond the lowest deciles to capture impacts on middle-income groups, whose perceptions of fairness often shape the political feasibility of reforms. Embedding such analysis more systematically into fiscal toolkits would help the Fund better integrate political economy considerations into its fiscal advice.

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CHAPTER 2—THE IMF'S ADVICE ON FISCAL RULES AND INSTITUTIONS

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

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EXECUTIVE SUMMARY

Fiscal rules and institutions have gained prominence in shaping policy outcomes over recent decades. In contrast, fiscal councils, which provide fiscal forecasts and oversight, remain less widespread and are a more recent development.

The IMF has played a significant role in shaping the discourse on fiscal rules and fiscal councils, with its advice evolving in tandem with academic research. Initially emphasizing simple numerical rules, the Fund's top-line guidance has since focused on balancing simplicity, flexibility, and enforceability. Recent general advice stresses countercyclical flexibility, advocating expenditure rules and fiscal anchors adjusted for economic cycles, aligning with academic thinking. The Fund's emphasis on expenditure rules has influenced how flexibility has been incorporated into fiscal frameworks in practice. A strong legal framework and institutional support are emphasized as key for enforceability of fiscal rules. One area where the Fund has notably tailored its approach to the unique circumstances of developing countries is in its macroeconomic policy framework for resource-rich developing economies. The Fund has also increasingly highlighted the value of independent fiscal councils in promoting rule adherence and forecast accuracy.

The Fund has developed comprehensive databases on fiscal rules and councils that have been vital for analysis, but these should be updated more regularly.

Attention to fiscal rules and councils in Article IV staff reports seems to have increased over time, though coverage varies across country groups. There has been a shift from advanced economies (AEs) to more focus on emerging market and middle-income economies (EMMIEs), but low-income countries (LICs) still receive limited attention. This may reflect assumptions about political will or capacity constraints in LICs, or simply a tendency to focus on countries where such frameworks already exist.

Technical Assistance (TA) has been a key channel for delivering the Fund's bilateral guidance on fiscal rules and institutions. LICs receive considerably less TA in this area compared to EMMIEs. This may stem from perceptions about enforcement challenges, staffing constraints for fiscal councils, or a lack of donor interest in funding such TA for LICs. Nevertheless, this imbalance raises questions about whether support should be more evenly distributed. TA has had mixed impact: it has contributed to rule adoption and improvements in some countries, but in others, it was either provided after rules were adopted or did not lead to implementation at all. TA seems more focused on refining existing systems than establishing new ones.

To enhance the relevance and impact of its advice on fiscal rules and institutions, the IMF could better integrate TA findings into Article IV reviews and make the assessment of fiscal rules and institutions a standard part of every review. This would ensure greater attention to these frameworks and their compliance, encourage tailored advice based on country-specific institutional capacity, and improve data collection. The Fund should also develop clearer guidance on how fiscal rules and councils should differ across varying country contexts, including

institutional capacity and income levels. Furthermore, the IMF would benefit from conducting additional comprehensive, data-driven analyses, with greater focus on rule compliance, the macro-criticality of fiscal frameworks, and the effectiveness of fiscal councils across diverse country context (e.g., institutional capacity, macroeconomic volatility) to better inform surveillance and TA.

I. INTRODUCTION

1. **Fiscal rules and institutions are important for policy outcomes and have come in for increasing attention in recent decades.** In the early 1980s, only five countries had formal fiscal rules. As of end-2024, an estimated 120 economies have adopted at least one fiscal rule. This corresponds to 63 percent of all IMF member countries (Figure 1, Panel A).[1, 2]

2. **By comparison, fiscal councils (independent bodies that typically provide fiscal forecasts, advice, and monitoring) are less prevalent and more recent.** According to the IMF's Fiscal Councils Dataset, 52 countries have fiscal councils. As of 2024, these were thus present in roughly 25 percent of IMF member countries (see Figure 1, Panel B). Of 52 countries with fiscal councils, only Korea, Nigeria, North Macedonia and South Africa do not have a fiscal rule.[3] In a majority of cases, the introduction of fiscal rules preceded establishment of a fiscal council. In only 11 cases (Austria, Belgium, Denmark, Georgia, Iran, Mexico, Netherlands, Serbia, Uganda, United States, and Vietnam) was the reverse true. Most fiscal councils have as part of their mandate and practice monitoring compliance with fiscal rules. While Australia, Canada, Kenya, Mexico, Uganda, and the United States have both a fiscal rule and fiscal council, it is not within the mandate of the council to monitor compliance with the rule.[4]

3. **Fiscal rules were first adopted by advanced economies (AEs), and later by emerging market and middle-income economies (EMMIEs) and low-income countries (LICs), while fiscal councils are most prevalent in AEs.** Panel C of Figure 1 shows separately the shares of AEs, EMMIEs, and LICs with one or more fiscal rule.[5] It illustrates how fiscal rules were adopted earlier in AEs; their number took off in the early 1990s coincident with ratification of the European Union's (EU) Maastricht Treaty and subsequent Stability and Growth Pact and then rose

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[1] According to the IMF's Fiscal Rules Dataset (more on which below), 90 percent of advanced countries had one or more fiscal rule as of 2024, compared to 61 percent of emerging markets and 48 percent of low-income countries. The dataset covers 120 countries. We treat the remaining 71 IMF members as possessing no fiscal rules (on the basis of private communication from the Fiscal Affairs Department), although we also raise some questions about the accuracy of this assumption below.

[2] These data, discussed further below, include both national and supranational rules, such as those applying to European Union countries and members of the Eastern Caribbean Currency Union, the East African Monetary Union, the West African Economic and Monetary Union, and the Central African Economic and Monetary Community.

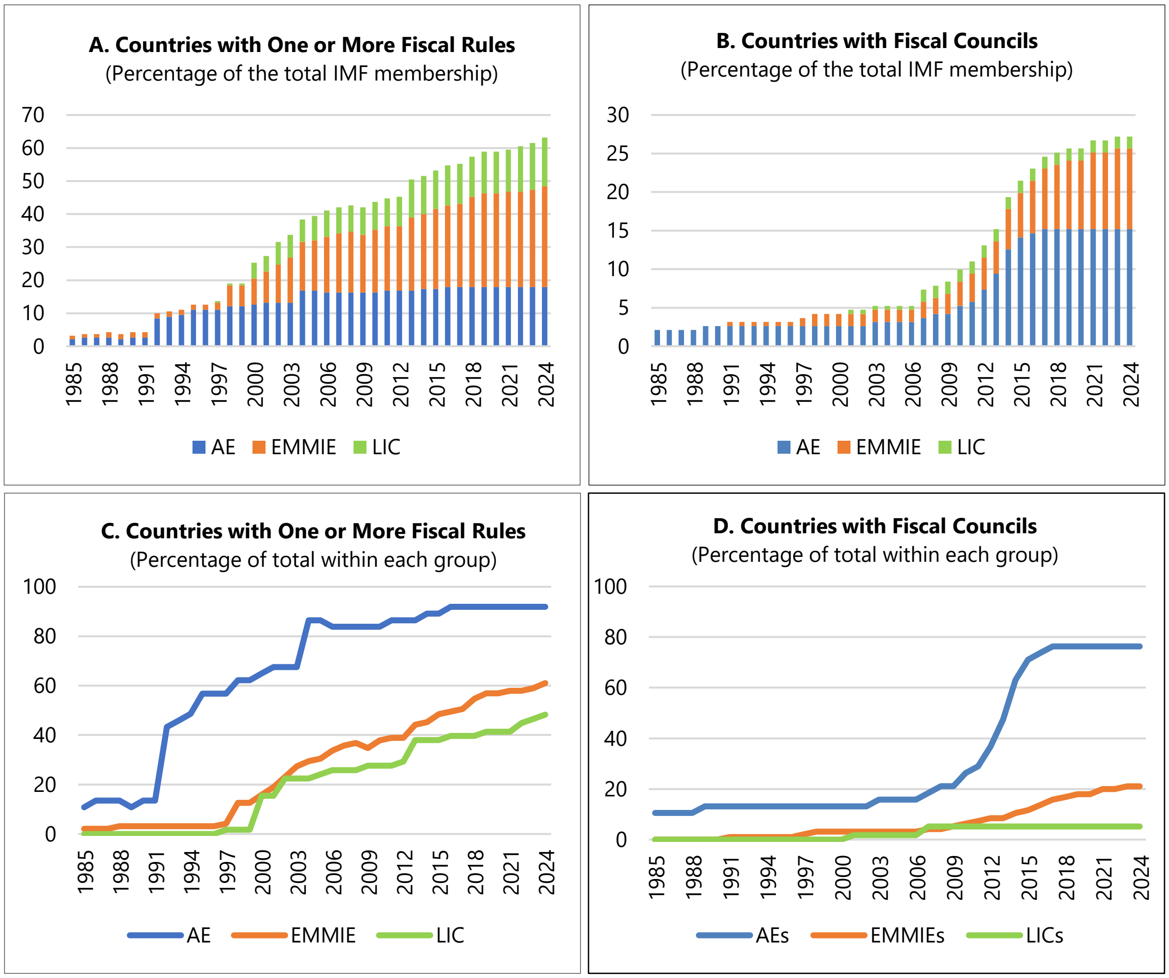
[3] In three countries (Belgium, Chile, Netherlands), there are two institutions performing the tasks of a fiscal council. In these cases, we used the year when the older one was established. In the case of the Netherlands, the institution that was established later (2014), not the one created in 1945, is responsible for monitoring compliance with fiscal rules. Thus, 92 percent of countries that have a fiscal council also have one or more fiscal rule. Of 120 countries with at least 1 fiscal rule, 48 have a fiscal council, which is 40 percent.

[4] As mentioned, Korea, Nigeria, North Macedonia and South Africa do not have any fiscal rules, so there is nothing to monitor. This leaves 42 countries where fiscal councils monitor compliance with fiscal rules (81–88 percent of all fiscal councils, depending on how these four countries are categorized).

[5] The chart in the appendix disaggregates these shares by type of rule (expenditure rule, revenue rule, budget balance rule, debt rule).

further from there.[6] The adoption of fiscal rules in EMMIEs and LICs develops somewhat later, around the turn of the century; adoption rises strongly from there. As of 2024, substantial shares of these country groupings have one or more fiscal rules in place. Fiscal councils' presence in AEs rose sharply following the Global Financial Crisis (GFC) of 2008–09 (Figure 1, Panel D). They remain less common in emerging markets (EMs) and (especially) LICs, where there was nonetheless some increase in prevalence in the most recent decade.

Figure 1. Fiscal Rules and Fiscal Councils in IMF Member States



Source: IEO staff calculations based on IMF Fiscal Rules Dataset and Fiscal Council Dataset.
Note: AE = Advanced Economy; EMMIE = Emerging Market and Middle-Income Economy; LIC = Low-Income Country. The number of countries within each group are 38 for AE, 95 for EMMIE, and 58 for LIC. For discussion of the datasets see Alonso and others (2025a, 2025b).

4. **This chapter evaluates the Fund's extensive analytical and policy work on fiscal rules and institutions which has been covered only marginally in previous evaluations or internal reviews.** It covers the period from 2008 to 2023 and assesses how the high level

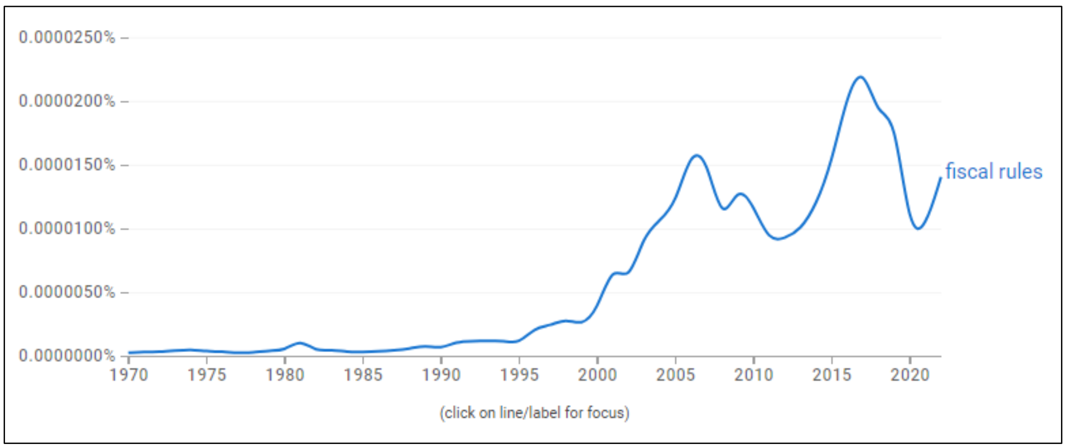
[6] The second upward shift in the mid-2000s reflects accession to the EU of additional Central and Eastern European members, who became subject to these same "Maastricht rules."

analytical and policy work translated into multilateral and bilateral recommendations. The chapter examines the Fund's advice in the context of surveillance, but also considers technical assistance (TA), given its relevance for certain income groups.

II. Policy Issues and Analytical Work on Fiscal Rules and Institutions

5. **The IMF's work on fiscal rules and institutions is part of broader attention paid to these aspects of fiscal management by the scholarly and policy communities.** Figure 2 summarizes the frequency of references to fiscal rules in the corpus of books digitized by Google. It shows a small increase in attention to the topic in the second half of the 1980s and first half of the 1990s, and then a sharp increase between 1996 and 2006, in part reflecting debate over the rules of the EU's Stability and Growth Pact, and in part reflecting greater attention to fiscal governance generally.

Figure 2. Frequency of References to Fiscal Rules



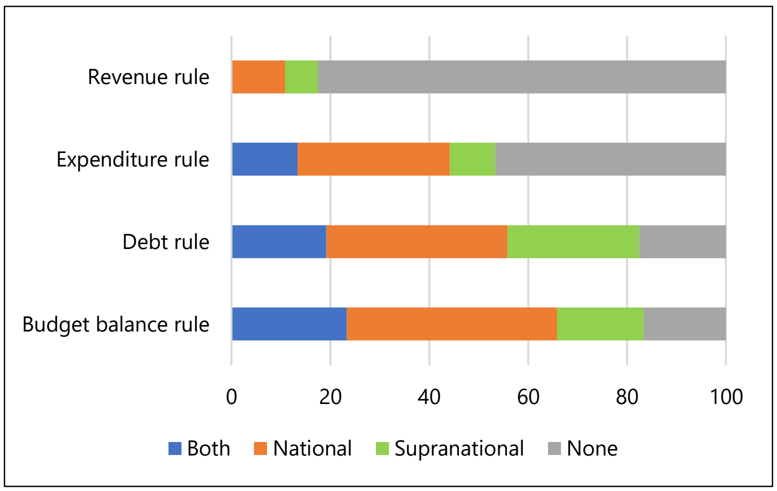
Source: Google Books Ngram Viewer.
Note: The figure was obtained by searching the keyword "fiscal rules" in the Google Books Ngram Viewer.

6. **The theoretical literature on fiscal rules is grounded in different workstreams.** These include the fiscal common pool problem (that the recipients of public spending fail to fully internalize the costs that taxpayers assume—see Krogstrup and Wyplosz, 2009), the political business cycle (that politicians seeking reelection or reappointment display deficit bias prior to elections, especially when electoral uncertainty is high—see Nordhaus, 1975; Tabellini and Alesina, 1990; Dubois, 2016), intergenerational burden sharing (that deficits now create burdens for future generations who lack a say in today's political process—see Wyplosz, 2012), and the so-called "debt dilution" problem (referring to the reduction in the expected repayment value of debt for existing creditors triggered by the issuance of new debt—see Hatchondo, Martinez, and Sosa-Padilla, 2016). Fiscal rules constraining the authorities' discretion are seen as militating against these deficit biases.

7. **An empirical literature seeks to quantify the incidence and strength of fiscal rules.** Early studies focused on U.S. states, 49 of which have balanced budget rules of varying strength (Poterba, 1997), or limited samples of AEs and emerging market and development economies (EMDEs) (Eichengreen and von Hagen, 1996). The European Commission (n.d.) now maintains a detailed database on numerical fiscal rules, fiscal institutions and fiscal frameworks for EU member states.[7] Badinger and Reuter (2015) have constructed indices of the stringency of fiscal rules for 81 countries covering the period 1985–2012. The most comprehensive database is the IMF's "Fiscal Rules Dataset," initially covering the period 1985–2015 and subsequently was updated through 2024 (see Davoodi and others, 2025). This includes 120 countries and distinguishes budget balance rules, debt rules, expenditure rules, and revenue rules.[8] Figure 3 shows the prevalence of these rules across IMF members (both the 120 members with rules and place and other countries).

Figure 3. Fiscal Rules by Type

(Percent of the total, as of 2024)



Source: IEO staff calculations based on FAD data.

Note: "Both" refers to cases where national and supranational rules coexist.

8. **Work surveyed by Brandle and Elsener (2023) analyzes the association of fiscal rules with fiscal outcomes.** Findings differ depending on country sample, period, specification, and how rules are measured (for example, whether a study distinguishes expenditure rules, revenue rules, balanced budget rules and debt rules). Brandle and Elsener summarize the literature as showing that fiscal rules are associated with improved budget balances, increased fiscal space,

[7] This provides retrospective measures starting in 1990.

[8] In addition, Ulloa-Suarez, Valencia and Guerra (2024) focus on escape-clause provisions in fiscal rules, constructing an index of the clarity of escape clauses for Latin American and Caribbean countries. There does not appear to be a comparable index for other parts of the world in the IMF database or elsewhere.

lower debts, and lower public spending volatility.[9] Governments subject to rules issue more accurate budget forecasts and enjoy better sovereign bond ratings. There is little evidence that rules depress public investment or increase the procyclicality of fiscal policy.[10]

9. **Recent research emphasizes that effects depend on the details of rule design.**[11] Dubrun and others (2008), Berman, Hutchison, and Jensen (2016) and Chrysanthakopoulos and Tagkalakis (2023) find that rules that apply to the general government, provide for cyclical adjustment, include a well specified escape clause, and are subject to strict enforcement and a strong legal base have stronger disciplinary effects. Nerlich and Reuter (2016) find a strong impact on fiscal space of expenditure rules, a weaker impact of budget rules, and no impact of debt rules. Ardanaz and others (2020) find that fiscal consolidation reduces public investment in countries with rigid fiscal rules but no reduction in countries where fiscal targets are adjusted for the business cycle, rules include a well-defined escape clause, or the rule excludes capital expenditure.[12] An IMF paper (Bova, Carcenac, and Guerguil, 2014) concludes that second-generation rules with cyclically-adjusted targets, well-defined escape clauses and strong enforcement are associated with less procyclicality.[13] Hatchondo, Martinez, and Roch (2022a, 2022b) propose a spread-brake rule imposing a ceiling on the fiscal deficit when the sovereign spread is above a threshold, as the spread itself summarizes information about the country's debt-carrying capacity.

10. **Some analyses suggest that the impact of fiscal rules depends not only on rule design but on country- and period-specific circumstances and the broader institutional framework.** Bergman and Hutchison (2015) and Ardanaz, Ulloa-Suarez and Valencia (2023) find that rules improve fiscal outcomes where institutional quality is strong. Gootjes and de Haan (2022) find that rules improve outcomes only where data on fiscal variables are good. Combes, Minea and Sow (2017) find that the impact of rules varies between low- and high-debt economies. Basdevant and others (2020) find that negative effects on public investment are attenuated by strong infrastructure governance and effective budget procedures. Hartwig and Sturm (2019) find that rules increase in income inequality, whereas Combes and others (2019) find a reduction.[14]

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[9] There are exceptions, such as Caselli and Reynaud (2020) who find that the effect of fiscal rules on the fiscal balance is insignificant overall, although there is some evidence that strong, well-designed rules have a positive effect. Heinemann, Moessinger and Yeter (2017) reach similar conclusions

[10] Again, not all studies agree. Lim (2020) finds that fiscal rules amplify procyclicality. Keita and Turcu (2022) find fiscal rules have no impact on procyclicality for countries with fixed exchange rate regimes, but that they reduce procyclicality for countries with flexible rates.

[11] On the definition of the fiscal target, rigidity versus flexibility, strength of enforcement, etc.

[12] Blesse, Dorn and Lay (2023) review 20 empirical studies and reach similar conclusions (that rigid rules depress public investment, whereas flexible rules do not).

[13] Guerguil and others (2017) reach similar conclusions.

[14] It may be relevant that Hartwig and Sturm analyze a sample of relatively advanced (EU) countries, while Combes and others (2019) consider a panel of 84 developing countries.

11. **The policy-oriented literature, including some from the IMF (see, for example, Kopits and Symansky, 1998; Basdevant and others, 2020), supplements this focus on numerical fiscal rules with attention to fiscal institutions and procedures.** This literature suggests that transparent budgeting processes, sometimes codified in the form of fiscal responsibility laws, are conducive to positive fiscal outcomes. These may require government to present a statement of its medium-term fiscal objectives, along with a medium-term fiscal framework that specifies public spending ceilings. Requiring authorities to report fiscal outcomes in timely fashion by publishing midyear and end-year fiscal reports enables independent monitoring of fiscal conduct by elected officials, investors and the public, which may again be conducive to positive fiscal outcomes. Obliging the government to present a medium-term fiscal framework encourages the authorities to internalize the budgetary implications of fiscal measures that go beyond the yearly budgetary cycle. These procedures can be given a legal basis through the adoption of Fiscal Responsibility Laws (Corbacho and Schwartz, 2007).

12. **Part of the literature focuses on independent fiscal councils.** Those are empowered to evaluate and monitor a government's fiscal plans and performance, provide non-partisan analyses of the long-term sustainability of the public finances, and make recommendations for adjustments in fiscal policy (Beetsma and Debrun, 2016). The theoretical argument for such councils is that by informing the public about fiscal policy in non-partisan fashion, they raise the reputational cost to politicians of undesirable fiscal policies. (See Calmfors and Wren-Lewis, 2011; Calmfors, 2015; Beeetsma and Debrun, 2016.) One variant holds that autonomous fiscal bodies are preferable to numerical rules: where rules can be rigid and arbitrary, council members can incorporate all relevant information about current and future circumstances, uninfluenced by partisan considerations and intertemporal distortions (Wyplosz, 2005). Another variant defends numerical rules and holds that rules and councils are complements rather than substitutes. Councils' forecasts and reports can verify the compliance of decision makers with numerical rules, again magnifying the reputational costs of noncompliance (Beetsma and Debrun, 2018).

13. **Focus on fiscal councils developed later than attention to fiscal rules (Figure 4).**[15] As with rules, there exist several databases on the incidence and characteristics of fiscal councils. Nerlich and Reuter (2013) provide data on fiscal councils for 27 EU countries in 1990–2012. The European Commission's dataset on fiscal rules in the EU provides information on fiscal councils as well. The most comprehensive such dataset, covering the period 1985–2024, is from the IMF (Alonso and others, 2025a).

14. **A body of empirical literature has examined the impact of fiscal councils.** Nerlich and Reuter (2013), using data for the EU, find that independent fiscal councils strengthen the positive impact of fiscal rules on the fiscal balance, supporting the hypothesis that rules and institutions are complements rather than substitutes. Fall and others (2015) obtain similar results for 30 OECD countries. Debrun and Kinda (2017), in an analysis written for the IMF, find that well-

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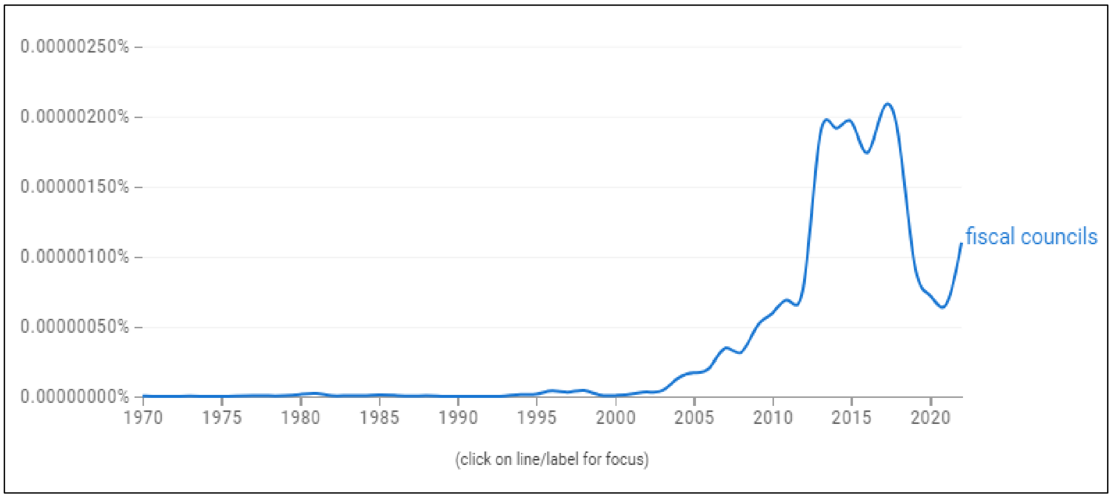
[15] It can be argued that attention to fiscal councils developed *in reaction against* the earlier adaption of fiscal rules, responding to the view that rules were arbitrary, procyclical or difficult to enforce.

designed fiscal councils are associated with better macroeconomic and budgetary forecasts. Beetsma and others (2019), also in an analysis written for the Fund, find that the presence of an independent council is associated with more accurate budget forecasts and compliance with rules. They conclude that council limit overoptimism in budget forecasts.[16] This study includes an analysis of what structures (such as legal independence) and responsibilities (as set out by the institution's mandate) are associated with improved fiscal and forecasting outcomes. It does not, however, compare the effectiveness of fiscal councils under different country conditions (different degrees of fiscal capacity etc.).

Figure 4. Frequency of References to Fiscal Councils



Source: Google Books Ngram Viewer.
Note: The chart was obtained by searching the keyword "fiscal councils" in the Google Books Ngram Viewer.

15. **As with the literature on fiscal rules, that on councils again suggests that the details matter for outcomes.** Debrun and Kumar (2008), using data for EU fiscal councils, find that these help to secure stronger budget balances only when sufficiently independent. Also, for EU countries, Capraru and others (2022) find that the impact of fiscal councils on the budget balance and compliance with numerical rules is greater where these entities have been present for an extended period, enabling them to gain experience and reputation. Chrysanthakopoulos and Tagkalakis (2023) find that fiscal councils contribute to fiscal adjustment when they have strong mandates (independence and a clear remit) and when they are strongly accountable.

16. **In sum, recent decades have seen the growth of a large literature on the fiscal rules and institutions that paints these as militating against political-economy sources of deficit bias.** Evaluations of their impact are broadly favorable, although studies emphasize that outcomes depend on legal and institutional specifics and may be contingent on country circumstances and the broader institutional environment.

[16] Gilbert and de Jong (2017) obtain the same finding.

III. IMF ADVICE ON FISCAL RULES AND INSTITUTIONS

General Policy Messages

17. **The Fund's views and advice on fiscal rules, fiscal councils and related matters have been disseminated through Board Papers, Staff Discussion Notes and Flagship Reports.**[17] Conversely, surveillance Reviews and associate Guidance Notes have covered fiscal rules and institutions to a limited extent (Box 1). Board Papers and Staff Discussion Notes on fiscal rules often appeared in conjunction with notable fiscal events. Thus, an early Board Paper on fiscal rules (IMF, 2009) appeared during the GFC, prompted by a "sharp increase in fiscal deficits and public debt in most advanced and several developing countries [that] has raised concerns about the sustainability of public finances…" It argued strongly that fiscal rules are associated with improved fiscal performance.[18]

Box 1. Fiscal Rules and Institutions in IMF Surveillance Reviews and Guidance Notes for Surveillance

Surveillance Reviews and associated Guidance Notes have covered fiscal rules and institutions only marginally. The 2008 and 2011 Triennial Surveillance Reviews (TSR) did not discuss fiscal rules and institutions, so the associated 2009 and 2012 Guidance Notes for Surveillance were silent on the topic (IMF, 2008, 2009, 2011, 2012). The 2014 TSR, on the other hand, recognized that the Fund's advice had emphasized the importance of fiscal institutions to help transition from short-term stimulus to medium-term consolidation in the aftermath of the Global Financial Crisis, and considered the design of institutional frameworks, including binding commitments, such as fiscal rules, as "crucial for policy credibility and effective implementation" (IMF, 2014). The 2014 TSR also assessed the extent to which advice provided in Article IV reports considered fiscal institutions. The subsequent 2015 Guidance Note for Surveillance indicated that Article IVs "should discuss fiscal institutions where relevant and take these into account when designing fiscal policy advice (IMF, 2015). However, it did not make recommendations regarding the coverage of fiscal rules and institutions in Article IV staff reports. One of the key recommendations of the 2014 TSR was that fiscal advice should be presented "in terms of a clear and well-justified anchor."[1] While this anchor in not necessarily an institutionalized, binding fiscal rule, this recommendation underscores Fund's view on the value of medium-term numerical targets. The 2018 Interim Surveillance Review and the 2021 Comprehensive Surveillance Review did not discuss fiscal rules and institutions (IMF, 2018a; 2021).

The most recent Guidance Notes covered fiscal rules very briefly. The 2022 Guidance Notes for Surveillance under Article IV Consultations listed fiscal institutions among elements that could be considered in providing policy advice, as relevant (IMF, 2022a). The most recent Staff Guidance Note on Engagement with Small Developing States, which was expressly designed to direct attention to the differentiated circumstances of such countries, made brief mention of the desirability of fiscal rules with a clear and credible fiscal anchor, provisions for adjusting targets in the event of shocks (which tend to be especially prevalent in many of these countries) and credible paths for returning to targets in the medium term (IMF, 2024a).

Source: IMF (2008, 2011, 2014a, 2015, 2018a, 2021, 2022a).

[1] The 2014 TSR clarified that the anchor could be specified in terms of either a fiscal (level) or adjustment (change) target to be achieved in 4–5 years.

[17] The latter "showcase policy-related analysis and research being developed by IMF staff…" and thus are directed at a broader audience of policy makers in member countries.

[18] It also emphasized the need for cyclical adjustment to limit procyclicality, the importance of comprehensive expenditure coverage, the need for effective monitoring and enforcement, and the alternative of independent fiscal institutions. A technical manual from the Fiscal Affairs Department (Bornhorst and others, 2011) then offered guidance on how to execute the cyclical adjustment.

18. **In response to the exceptional COVID-19 crisis, the Fund published timely analyses on frameworks that incorporate greater flexibility within fiscal rules.** An FAD paper focused on the need for escape clauses that provide flexibility without undermining the credibility of rules (Gbohoui and Medas, 2020).[19] A Staff Discussion Note (Caselli and others, 2022) highlighted how the temporary suspension of fiscal rules and heightened debt loads offered an opportunity to re-think debt rules. It cautioned that numerical rules could be either overly rigid or unrealistically complex. It recommended less reliance on annual budgets, more attention to medium-term plans, steps to enhance budgetary transparency, and strengthening the role of fiscal councils.[20]

19. **Of the Fund's flagship publications, fiscal rules and institutions have received attention mainly in the Fiscal Monitor (FM) (Figure 5).** Mentions of specific country arrangements are included, as are special features considering rules, institutions and procedures more generally (special features account for most of the spikes in Figure 5).

- The April 2013 FM included a box on fiscal councils that operate independently of the government and benchmark their assessments to the government's objectives so as to avoid being drawn into partisan debates. This discussion built on a policy paper (IMF, 2013) finding that presence of a fiscal council tends to be associated with stronger budget balances and less procyclical policies so long as the council enjoys legal and/or operational independence, is responsible for monitoring compliance with fiscal rules, has strong media presence, and follows procedures that are efficiently sequenced with the budget process.[21]

- The April 2014 FM included an appendix on expenditure rules, arguing that these displayed a better record of compliance than debt and balanced-budget rules, but that they might encourage cuts in public investment in bad times. This analysis was useful and important. However, there have been few subsequent analyses by Fund staff of compliance and violations, disaggregated by type of rule and macroeconomic and financial circumstances.

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[19] This paper built on a pair of earlier Staff Discussion Notes (Eyraud and others, 2018; Caselli and others, 2018) emphasizing the desirability of three properties: simplicity, flexibility and enforceability. Staff included also discussion of independent fiscal councils as a factor in improving enforceability.

[20] The note builds in part on an earlier working paper by some of the same authors (Davoodi and others, 2022c).

[21] The *Fiscal Monitor* (FM) also discussed caveats. It cautioned that fiscal councils are effective only if policy makers have already internalized the merits of fiscal discipline (without, however, alluding to the possibility that presence of a fiscal council is only capturing the effects of this internalization). It observed further that councils are effective only when they possess a critical mass of expertise and resources (without explicitly alluding to the fact that this institutional approach may be least effective in low-income countries). Moreover, whereas some academic literature (e.g. Fatas and others, 2003; Wyplosz, 2005) had suggested substituting fiscal councils with decision making powers for fiscal rules, IMF (2013) expressed skepticism about the political viability of fiscal councils "with teeth." It suggested that fiscal councils are better thought of as complements than substitutes for fiscal rules, effectively as monitoring technologies for the government's compliance with its fiscal rules. It observed that as of 2013 about 80 percent of countries with fiscal councils also had numerical rules, that in most cases the establishment of fiscal councils followed the adoption of numerical rules, and that in three-quarters of these cases the council is mandated to monitor compliance with those rules.

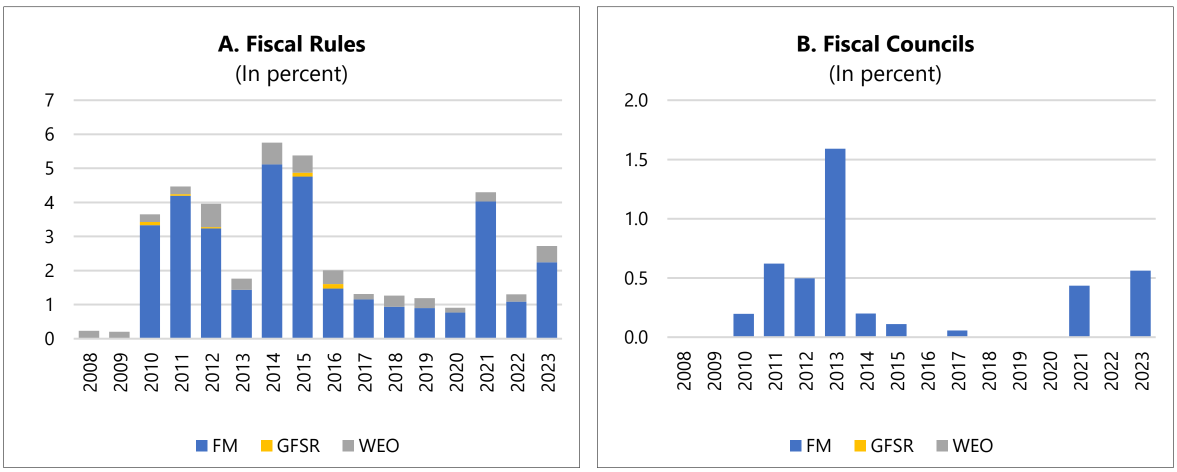
- The October 2015 FM then focused on commodity exporting countries, highlighting how fiscal rules could limit procyclicality in response to resource booms, and indicating that rules should take account of volatility and uncertainty about commodity prices.[22]

- The April 2021 FM highlighted the flexibility and temporary suspension of fiscal rules during the pandemic and recommended strengthening rules in light of heavier debt loads.

- The October 2021 FM emphasized the need to restore fiscal balance and credibility following the pandemic, highlighting the desirability of restoring temporarily suspended fiscal rules.[23]

Figure 5. Frequency of References to Fiscal Rules and Fiscal Councils in Flagship Publications

(Proportionate to total number of paragraphs within flagship)



Source: IEO staff calculations based on SPR data.

Note: The list of keywords used in text analysis is reported in the Appendix II. Panel B shows the percentage of paragraphs referencing fiscal councils in the total number of paragraphs in *Fiscal Monitors* published in a given year. There were no references to fiscal councils in GFSR and WEO during the period covered by the evaluation.

20. **IMF working papers discussing fiscal rules have been fairly numerous (Figure 6)**.[24] Attention to rules increased around the time of the GFC and the Greek and Euro Area debt crisis and remained fairly stable until the outbreak of the COVID-19 pandemic.[25] Analysis of fiscal councils was more sporadic and generally came later.

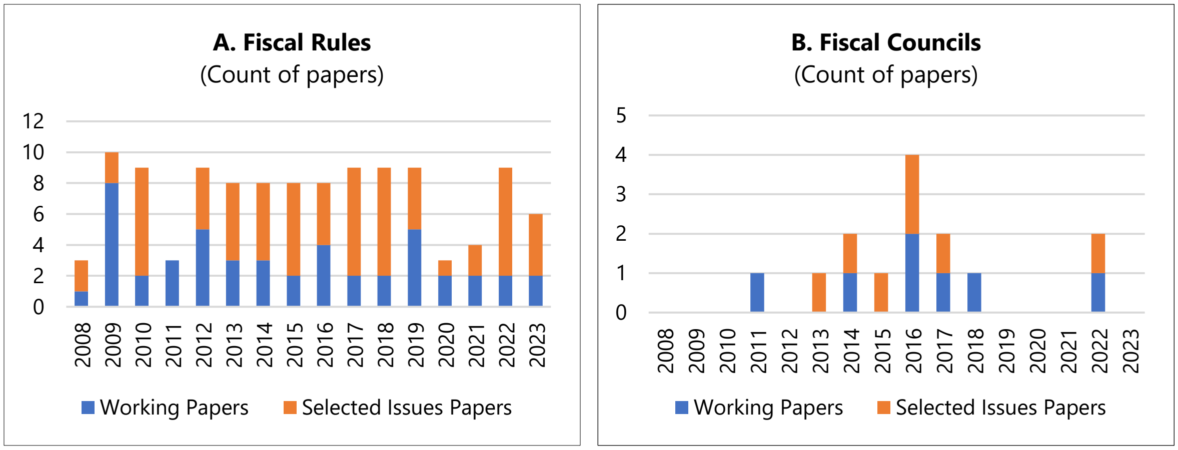
[22] These passages account for the 2014 and 2015 spikes in Figure 4.

[23] Recently, and beyond the period covered by this evaluation, the October 2024 FM provided evidence that countries with fiscal rules have lower debt-at-risk (defined as the 95th quantile of projected debt) and smaller unidentified debt during periods of banking crisis.

[24] Expressing this as a percentage of all working papers in the year shows the same pattern.

[25] The spike in 2009 corresponds to initial publication of the IMF's fiscal rules database.

Figure 6. IMF Working Papers and Selected Issues Papers on Fiscal Rules and Fiscal Councils



Source: IEO staff calculations.

21. **The Fund has gone some way in distinguishing the position and response of AEs, EMs and LICs.** A 2009 Board Paper (IMF, 2009) noted that AEs are more likely to have a fiscal council or other independent monitoring agency, while EMs are more likely to have a fiscal responsibility law. It observed that LICs were least likely to adjust the budget balance for the cycle and most likely to exclude investment spending from the fiscal target. It did not, however, provide an explanation or analysis of these differences. Nor did it analyze whether such differences were appropriate to differing national circumstances. In its analysis of compliance with fiscal rules, the spring 2014 *FM* distinguished the compliance of AEs and EMs, without however providing an explanation for observed differences.[26] The fall 2021 *FM*, in its discussion of escape clauses and the reactivation of fiscal rules following COVID-19, did not devote significant attention to differences between AEs and EMDEs. Area departments (e.g., the African Department (AFR) and the Asia and Pacific Department (APD)) have produced papers analyzing fiscal rules in certain regions (Comelli and other, 2023; Flores and others, 2024).

22. **One area where the Fund has paid special attention to the differentiated circumstances of developing countries is in its macroeconomic policy framework for resource rich developing countries (RRDCs) (Baunsgaard and others, 2012; IMF, 2012).** This report, a collaboration between multiple IMF departments and the World Bank, considered advice tendered to 29 developing countries rich in non-renewable natural resources. The report noted that in only about half of RRDCs had the Fund recommended the introduction of a fiscal rule to smooth spending volatility. The Fund's advice on short- to medium-term rules focused mainly on non-resource fiscal balance rules, and less on price-based rules that relate the fiscal balance to resource-price fluctuations. While some 40 percent of the RRDCs considered used a

[26] The Fall 2015 *Fiscal Monitor* distinguished resource-rich countries, providing a separate discussion of the appropriate design of fiscal rules. Although there are both advanced and emerging market/low-income countries under this heading, in practice the question of managing the fiscal implications of natural resource wealth is disproportionately an emerging market/low-income country issue.

resource reference price when budgeting, their practices did not in general extend to the adoption of an explicit fiscal rule (they do not adopt explicit deficit targets). Attention was paid in Fund advice to RRDCs on how to strengthen public financial management, including creating a resource fund or sovereign wealth fund and adopting a medium-term expenditure framework for multi-year budgeting, but there does not appear to have been much if any discussion of the possible creation of fiscal councils in this context.[27] A more recent working paper revised the advice to resource-rich countries calling instead for establishing fiscal buffers and a medium-term anchor, based either on net financial assets as a share of annual commodity revenues, or on outstanding public debt (Eyraud and others, 2023).

23. **A Staff Discussion Note (Eyraud and others, 2018) presented a comprehensive view on the design and effects of fiscal rules.** It presented informal evidence that well-designed rules are effective in constraining excessive deficits. It defined well-designed rules as simple, flexible and enforceable. It found that recent rules moved in the direction of increased flexibility, broader sanctions and stricter oversight, but also greater complexity. It recommended combining a medium-term debt target or anchor with a single operational rule for annual fiscal policy; an expenditure rule, a revenue rule, or a balanced-budget rule—though it did not endorse one of these alternatives as preferable to the others. It recommended provisions allowing for flexibility over the cycle, which led to a preference for expenditure rules (placing a ceiling on expenditure while allowing revenue to fluctuate as a way of providing countercyclical flexibility). Though now more than five years old, this formulation appears to summarize the current internal state of play.[28]

Bilateral Advice

24. The IMF provides bilateral advice on fiscal rules, procedures and institutions in conjunction with Article IV missions and reports and via TA.

Surveillance

25. **Attention to fiscal rules and councils in Article IV staff reports seems to have increased over time.** One way of gauging IMF engagement is to ask in what share of Article IV reports there is any mention of fiscal rules and councils. Figure 7 shows the relevant percentages. This shows an ongoing if unsteady increase from 2009. Again, references to fiscal councils rise later. Notice also the contrasting scales of the two panels; fewer Article IV reports mention fiscal councils.

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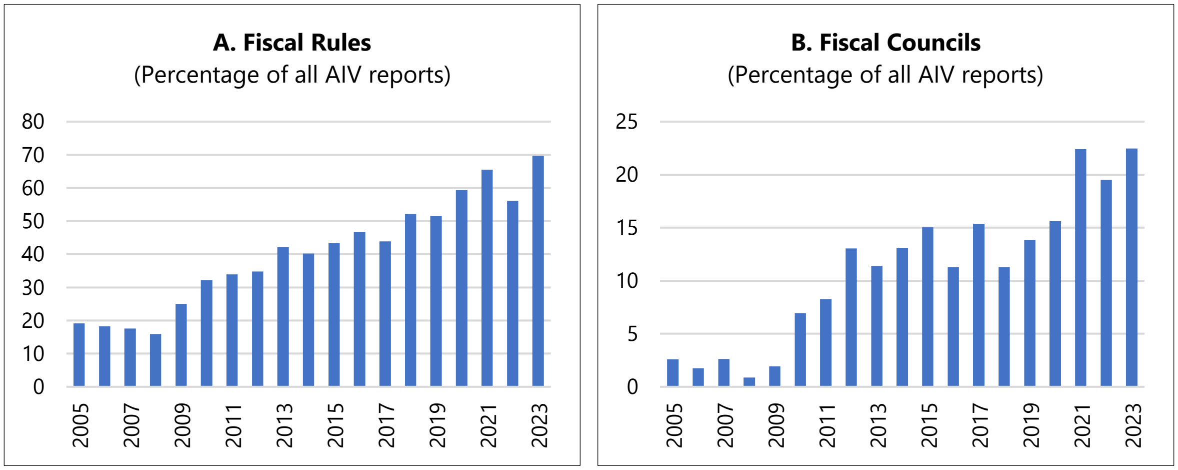
[27] In a small number of the cases considered, the Fund pointed to the possible adoption of a fiscal responsibility law (in the context of which a fiscal council might be created). But the report concluded (p. 43) that "The Fund could also do more to help RRDCs build the necessary institutions, including fiscal responsibility laws."

[28] To provide more operational guidance on fiscal rules and institutions, FAD prepared two hands-on How-To-Notes, focusing on how to select fiscal rules in AE, EMMIEs, and LICs and rule calibration, respectively (IMF, 2018b; 2018c). Akanbi, Gbohoui, and Lam (2023) provided a tool in calibrating fiscal rules considering natural disaster risks. FAD also produced a How-to-Note on how to develop and implement medium-term fiscal frameworks (IMF, 2024).

Figure 7. Article IV Reports Containing At Least One Reference to Fiscal Rules and Fiscal Councils



Source: IEO staff calculations based on FDET data.

26. **Text analysis indicates that the frequency of references to fiscal rules and councils in Article IV reports varies across country group (Figure 8).**[29] In the first part of the period, 2008 to 2013, reference was made most frequently in AE Article IV reports, followed by EM Article IVs, and relatively infrequently in LIC Article IVs. This early period featured the GFC, which centered disproportionately on those same AEs, many of which responded by applying significant fiscal stimulus, followed by efforts at fiscal consolidation. Subsequently, more regular mention is made of fiscal rules in EMs, but attention to fiscal rules in LICs remains infrequent. This imbalance may be influenced by the fact that AEs were early adopters. The Fund turned its attention to the design and operation of fiscal rules in emerging markets as the EMs in question put such rules in place. Similarly, the Fund may devote relatively little attention to fiscal rules in LICs because few LICs have adopted them. Article IV reports appear to devote more attention to how members might strengthen and refine existing rules than to how members lacking such rules might design and implement them, though TA supported adoption of fiscal rules in some cases (see below). Figure 8 also shows that discussion of fiscal councils focused relatively heavily on AEs in the period 2009-11, when the Fund seems to have paid particular attention to the institution in bilateral surveillance. Subsequently, the proportion of Article IV discussion devoted to the arrangement declined, while the focus shifted to EMs.

27. **Country cases suggest that treatment of fiscal rules and procedures in Article IVs is uneven (Box 2).** In some cases where rules exist, they are discussed extensively, and detailed recommendations for refinement are provided. In other cases, in contrast, they are not discussed at all. In addition, we took a selection of advanced, emerging and low-income countries that repeatedly breached their national fiscal rules over the period starting in 2015. In some cases,

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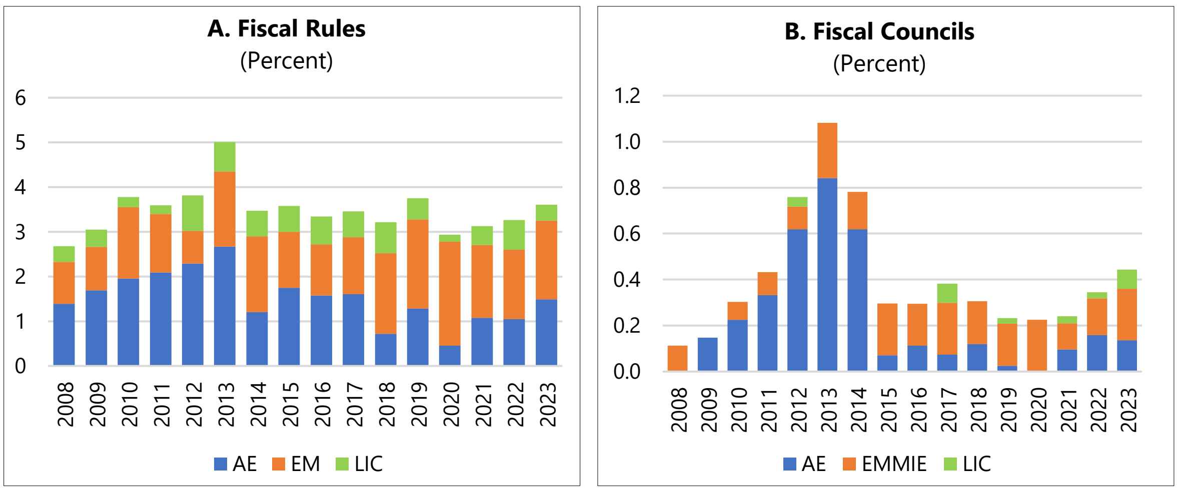
[29] Figure 7 includes references in Article IV reports but excludes references in Special Issues Papers (SIPs). The number of Special Issues Papers (attached to Article IV reports) that discuss fiscal rules again show a similar temporal pattern.

Staff pointed to violations of their fiscal rules, but in others the existence of rules was not mentioned. The latter was the case of Pakistan and Sri Lanka, for example. Pakistan was in Extended Fund Facility (EFF) programs in 2013–16 and 2019–22, respectively. Staff consultation reports for Pakistan in this period focused on evaluating whether or not the country was meeting its annual targets. Similarly, for Sri Lanka reports focused on budgeted deficits and whether the authorities were able to meet these. In Nigeria, the Staff did not account for the country's fiscal rules in the 2015 to 2020 period analyzed.

Figure 8. Frequency of References to Fiscal Rules and Fiscal Councils in Article IV Reports by Country Group

(Proportionate to total number of paragraphs within Article IV reports)



Source: IEO staff calculations based on SPR data.
Note: The figure shows the percentage of paragraphs referencing fiscal rules or fiscal councils in the total number of paragraphs in all Article IV reports published in a given year. AE = Advanced Economy; EM = Emerging Market; EMMIE = Emerging Market and Middle-Income Country; LIC = Low-Income Country.

28. **The Fund has provided advice also on supranational rules, most notably on the EU fiscal governance.** Advice to the EU was offered as part of the IMF annual consultation with EU institutions as well as through the *FM* and other publications.[30] Most recently, the Fund has expressed its recommendation for the EU fiscal framework in a major inter-departmental project (Box 3). However, Article IV reports on EU member states generally make only very brief mention of EU fiscal rules when assessing members' fiscal plans and performance. Other economic and monetary unions (the Eastern Caribbean Currency Union, the East African Monetary Union, the West African Economic and Monetary Union, and the Central African Economic and Monetary Community) also have fiscal rules in place, either anchors for debts and/or operational rules for revenues or deficits. Mention of these fiscal rules in Article IV reports are uneven. We reviewed 35 available Article IV reports in the period 2015–20, finding that supranational rules are mentioned in 16 of them (46 percent).

[30] See, for example, FM November 2010 (Box 3.2), April 2011 (Box 4.1), April 2012 (Box 5), October 2012 (Box 6).

Box 2. Country Cases in Article IV Reports

Country cases suggest that treatment of fiscal rules and procedures in Article IVs is uneven. Consider Bahamas and Vietnam.

- **Bahamas** introduced a fiscal rule and established a fiscal council in 2018. A first mention of this possibility in an Article IV comes in 2017, when staff welcomed "the authorities' intention of adopting a fiscal rule" and provided a paragraph on basic design concepts.[1] The 2018 Article IV then described appropriate calibration of the rule, recommending a debt ceiling or anchor of 50 percent of GDP, an annual deficit target of ½ percent of GDP and a cap on the growth rate of current expenditure of 3 percent. It noted that legislation was being prepared with Fund technical assistance (IMF, 2018d). Although the legislation adopted differed from these particulars, the 2019 Article IV report, in a box describing the new Fiscal Responsibility Law, noted that the country's fiscal rules were "consistent with previous staff advice." There was little discussion of the country's fiscal council, however.
- **Vietnam** saw rapidly rising government debt around the middle of the last decade. The country maintained a rule limiting public and publicly guaranteed debt to 65 percent of GDP. FAD prepared a detailed analysis of this rule; this analysis recommended lowering the debt limit from 65 percent to 55 percent and supplementing it with an expenditure rule (IMF, 2017). The analysis was presented at a seminar at the Ministry of Finance. Yet there was no reference to this recommendation, and indeed no mention of the country's fiscal rule, in Article IVs for this or surrounding years.

The IMF has not been reticent about drawing attention to imperfectly designed fiscal rules.

- **Germany** 2024 Article IV criticized the country's debt-brake rule as requiring an "unnecessarily fast pace of debt reduction, especially when debt sustainability risks are low" and "excessive adjustment in years like 2024 when the escape clause is not activated…" It recommended raising the deficit limit to make more room for public investment. That said, the Fund was relatively late to the game: similar recommendations had already been issued by the German Council of Economic Experts and the Deutsche Bundesbank. The Fund did not criticize or otherwise comment on the debt brake in its 2010 and 2011 Germany Article IVs, the first such consultations after the debt brake was adopted.
- **Peru** 2019 Article IV provided analogous advice. This emerging market has had a Fiscal Responsibility and Transparency Law since 2003 and a fiscal council since 2016. Staff suggested that the country's 1 percent of GDP headline deficit target was constraining infrastructure investment. It recommended a "modest" increase in that deficit target while retaining existing rules limiting the growth of current expenditure, ensuring that the additional space under the revised deficit rule was used for investment.[2] No numbers defining "modest" were provided, however.
- **Brazil** 2023 Article IV staff report is another example. The country has had fiscal rules since 1988 and a fiscal responsibility law since 2000. IMF staff proposed enhancements to the new rule proposed by the authorities to replace an earlier constitutional spending ceiling (passed by the Brazilian National Congress a few months after the Article IV consultation). The report recommended reforming limits on spending to render them consistent with separate targets for the primary budget balance; adding a binding multi-year target path to guide the budget process over a longer horizon with an explicit fiscal anchor; reducing procyclicality by linking spending growth to sustained increases in revenues; computing and publishing separate cyclical and structural components of revenues; introducing an escape clause to be invoked in response to major shocks; and taking steps to strengthen the existing independent fiscal "watch dog," with adequate resources and independence. This is an ambitious set of reforms to propose to any country. It could be argued that it lacks a sense of prioritization.

Sources: IMF (2017, 2081d); Article IV Reports.

[1] It recommended a ceiling for the deficit, a cap on current expenditure growth, the formulation of medium-term fiscal projections, and an escape clause.

[2] As an alternative, the staff report suggested replacing the headline deficit ceiling with a structural deficit ceiling. In fact, Peru had replaced an earlier structural balance rule with a headline deficit rule in 2016 "against previous IMF advice," according to the 2017 Article IV report. While cautioning that the new rule could add procyclicality, the 2017 report commended it for transparency and inclusion of appropriate escape clauses. In addition, it is not obvious that these alternative recommendations are in fact alternatives, since enabling more infrastructure investment addresses a secular need, while targeting the structural deficit addresses cyclicality.

Box 3. IMF Advice on EU Fiscal Rules and Institutions

IMF advice on EU fiscal rules and institutions does not fall neatly under either multilateral or bilateral headings. A recent paper (IMF 2022b), a collaboration of the European, Fiscal Affairs, and Strategy, Policy and Review Departments, became the official IMF submission to the European Commission on reform of the Union's fiscal rules. The paper criticized the EU's existing fiscal rules for failing to contain fiscal risks while also failing to stabilize output. But it also affirmed the desirability of retaining the EU's existing 3 percent and 60 percent reference values for the deficits and debts of member states.

When considering the desirable pace of convergence to these ratios, it put a proposal for a new and independent European Fiscal Council at the center of its advice. This council, it suggested, should be tasked with developing a common methodology for assessing the debt sustainability of member states, and then with producing recommendations for the speed and ambition of fiscal consolidation based on the fiscal risks indicated by that methodology. This EU-level or EU-wide analysis would be a vehicle for taking into account negative externalities across member states when programming the speed and ambition of consolidation—negative externalities not accounted for in the preexisting framework.

Building on the advice of this European Fiscal Council, member states would then enact multi-year medium-term fiscal frameworks consistent with convergence to the EU's debt and deficit reference values. These frameworks would be operationalized by setting an expenditure ceiling at the national level. They would be monitored by strengthened and upgraded independent national fiscal councils tasked with undertaking or endorsing macroeconomic projections and performing their own debt sustainability analyses. The European Commission for its part would continue to conduct surveillance and would now also coordinate a peer network of national fiscal councils.

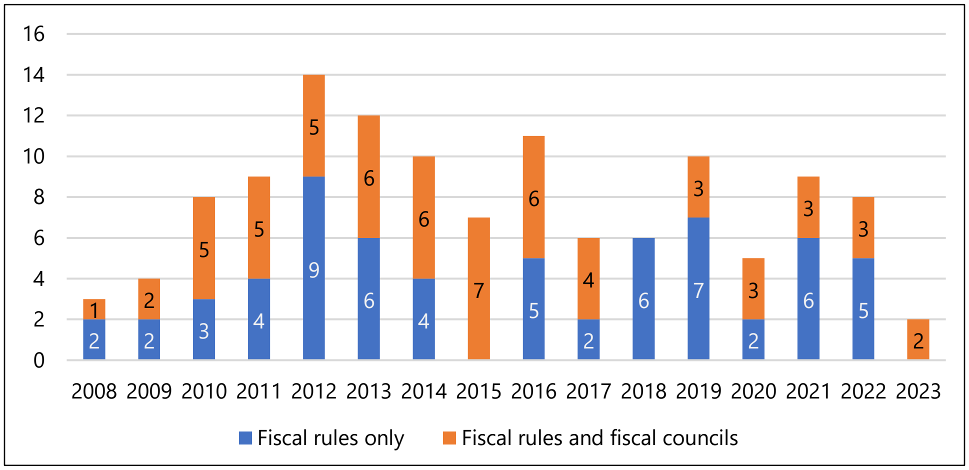
The recommendation of the IMF (and others) to supplement the EU's 60 percent and 3 percent debt and deficit anchors with a single operational expenditure rule was then adopted in the most recent revision of the EU's fiscal rules. The recommendation to create a European Fiscal Council was not acted upon. The EU has, however, established and renewed a more limited European Fiscal Board charged with advising on the prospective fiscal stance appropriate for the euro area as a whole, providing ex post evaluations of the implementation of the EU's fiscal governance framework and Stability and Growth Pact (including on appropriateness of activating and extending its general escape clause), and making suggestions for the future evolution of the fiscal framework.

Source: IMF (2022b).

Technical Assistance

29. **TA has served as an important instrument for delivering the Fund's bilateral advice on fiscal rules and institutions.** Fund's TA in this area covers a variety of issues, including, for instance, the identification and calibration of the more desirable rule, the legal requirements for the integration of the fiscal rule into the budgeting process, as well as the institutional design and related legal aspects for the creation and functioning of fiscal councils. We are aware of 126 TA reports in the review period that mention fiscal rules. The list was provided by FAD and meant to be exhaustive. Nearly half of these reports also referred to fiscal councils (Figure 9). There is no obvious trend or pattern when these TAs were conducted. For example, as many TAs were completed in the first half of the period (2008–15) as in the second (2016–23).

Figure 9. TA Reports Referring to Fiscal Rules and Fiscal Councils



Source: IEO staff calculations based on FAD data.

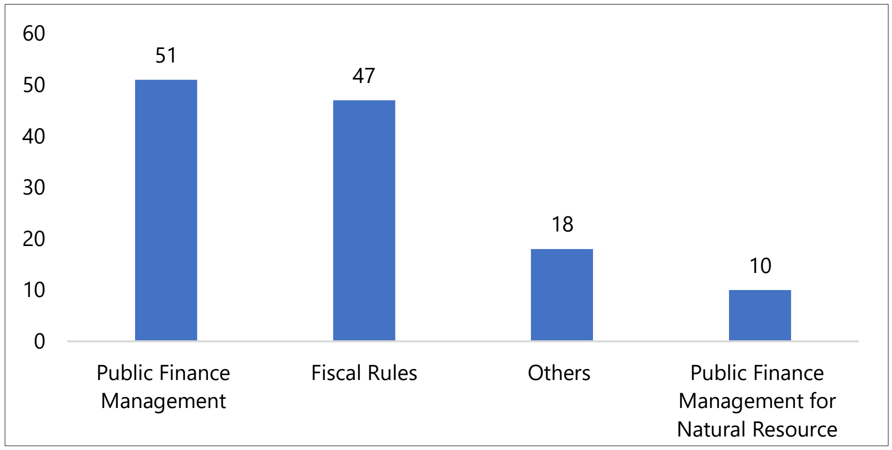
30. **Overall, 68 countries (about one-third of total IMF membership) received TA on these issues over 2008–23.** Some sought TA multiple times, while others received it only once. Peru received TA touching on these issues five times between 2011 and 2014; Serbia received it five times between 2010 and 2017. Another 13 countries received TA 3 to 4 times; 20 countries took TA twice; and the remaining 33 countries received TA only once.

31. **Of these TA reports, about 40 percent are primarily concerned with fiscal rules or fiscal councils.** The rest focus on Public Finance Management (PFM) but include a reference or passing advice regarding fiscal rules and councils. For example, the TA report on India in July 2018 is called "Reinforcing the Budget as a Main Policy Instrument." It does not provide specific recommendations on fiscal rules or fiscal councils. It only goes as far as advising a top-down budgeting process and recommending setting aggregate expenditure limits in the budget in line with policy priorities, macro-fiscal projections, and medium-term fiscal rules (not specified).

32. **These TA reports can be placed in four categories.** They comprise (i) those concerned with PFM; (ii) those concerned with fiscal rules, some of which also make reference to fiscal councils (there are no separate TA reports on fiscal councils); (iii) those concerned with public finance for natural resource dependent economies; and (iv) those concerned with other issues (examples include "Colombia—A Framework for Analyzing Long-Term Fiscal Projections and Pension Reforms, June 2012;" "Indonesia- Resolving End-of-the-year Cash Pressures, May 2017;" and "Panama- Fiscal Advice on Establishing A Sovereign Wealth Fund, April 2011"). Of 126 TAs, 51 were on PFM, 47 on fiscal rules, 10 on managing public finance for natural resource dependent economies, and 18 on other issues (see Figure 10). There is no obvious time pattern in their relative importance.

33. **Nearly half of TAs were provided in conjunction with an IMF program.** Members must request TA in order for it to be provided. It may be that the existence of a program alerts country officials to the availability of advice, or that IMF staff involved in the problem encourage the request.

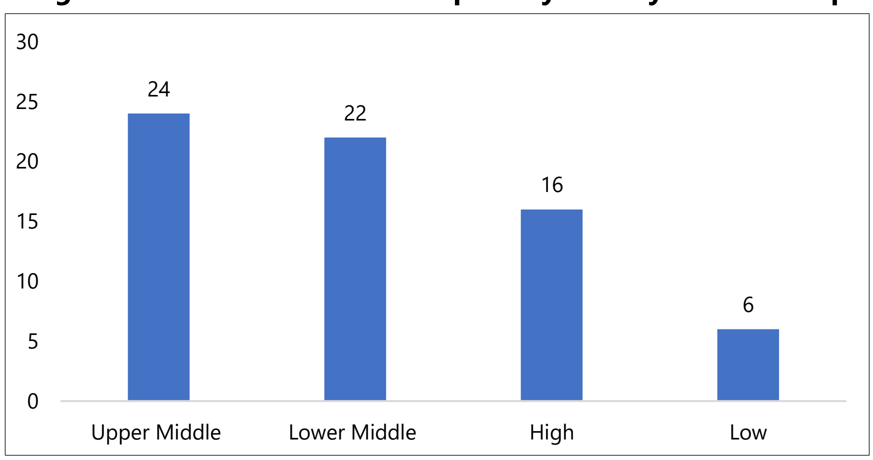
Figure 10. Technical Assistance Reports by Area of Focus



Sources: FAD and IEO staff calculations.

34. **Utilization of TA on fiscal rules and fiscal councils by member countries is uneven.** High income countries have received TA on these aspects more often than LICs. Use of TA by LICs has not increased over time. Of countries which have received TA touching on fiscal rules, 16 were high income, 24 upper-middle-income, 22 lower-middle-income, and only 6 low-income (Malawi, Mozambique, Sierra Leone, South Sudan, Tanzania, and Uganda) (Figure 11).[31] The fact that TA reports touching on fiscal rules are less common among LICs parallels what we find for Article IV reports. This may reflect the limited effectiveness of fiscal rules in these economies, where weak PFM capacity or political economy constraints prevail. In such contexts, Article IV consultation discussions and TA are more often directed toward strengthening PFM and developing—or introducing—medium-term fiscal frameworks.

Figure 11. Technical Assistance Reports by Country Income Group



Sources: FAD and IEO staff calculations.

[31] Income groups are as per the World Bank's classification in 2015. In 2015, low income economies are those with a GNI per capita of $1,045 or less; middle-income economies are those with a GNI per capita of more than $1,045 but less than $12,736; high-income economies are those with a GNI per capita of $12,736 or more; low-middle- income and upper-middle-income economies are separated at a GNI per capita of $4,125. (https://documents1.worldbank.org/curated/en/408581467988942234/pdf/WPS7528.pdf)

35. **In some cases, TA led to significant improvement and refinement of members' fiscal rules and framework.** Boxes 4 and 5 describe the positive examples of St. Vincent and Grenadines and of Jamaica. More broadly, however, it is difficult to determine how frequently advice provided via TA was implemented by recipient countries. One can compare advice in TAs to the IMF's databases on fiscal rules and fiscal councils (Davoodi and others, 2022c). Based on the timing of the TA and the implementation of fiscal rules and fiscal councils, one can draw plausible causal link in only a few cases. A positive example is Uganda, which was provided TA four times between 2010 and 2019.[32] It first adopted a fiscal rule in 2013. The 2019 TA recommended changes to the existing fiscal rule (specifically, setting an interim debt to GDP target and adding a mechanism to manage oil revenue flows). These recommendations were then added to Uganda's Charter for Fiscal Responsibility starting in fiscal year 2021–22.

Box 4. Technical Assistance on Fiscal Rules: The Case of St. Vincent and Grenadines

St. Vincent and Grenadines was the subject of a pair of TA missions in quick succession in 2021 and 2022 which helped to strengthen the existing framework.[1] The first TA, provided by FAD In April 2021, outlined measures to enhance the execution of the FRF. Recommendations related to technical issues such as coverage and definitions of key terms, strengthening the role of the Medium-Term Economic and Fiscal Outlook (MTEFO) in the budget process by formalizing the budget calendar, and ensuring underlying Public Financial Management systems and procedures were enshrined in legislation. With regard to the escape clause for the fiscal rule, the TA recommended that the Minister be required to submit to the Parliament the confirmation of suspension events, their impacts, and supporting data.

Economic distress in the aftermath of a volcanic eruption in 2021 led the government to seek a second TA in August 2021 which ended in January 2022. The TA reported that some progress had been achieved and provided additional recommendations on improving budgetary processes. These recommendations were taken on board by the authorities. It provided further recommendations on improving recurrent and capital budgeting processes, enhancing the role of the MTEFO, and clearly establishing the role of the FRM in transparent, timely, and comprehensive review of compliance with fiscal targets. It also suggested revising the debt target to align with the Eastern Caribbean Central Bank guideline of 60 percent debt/GDP ratio by 2035.

Following this, the government released its first FRM Report in November 2022, incorporating the recommendation of the 2022 TA on debt rule. In line with FAD's suggestion of increasing the role of the Cabinet in enforcing fiscal constraints, the report mandated a charter for budget management where all extra-budgetary funding requests involving resource implications would require the legal approval of the Budget Review Sub-Committee of the Cabinet. The report reiterated certain earlier recommendations such as enforcing a formal budget calendar (FRM Report, 2022).

The 2024 IMF staff Article IV report praised the authorities' continued commitment to reaching the debt target and the medium-term fiscal strategy set out in 2021. It acknowledged the country's efforts to build more efficient and equitable expenditure frameworks, to enhance revenue administration, and strengthen fiscal institutions while maintaining further improvements in the FRF are required to stabilize the path to multi-year fiscal discipline.

Sources: IMF TA reports.

[1] These were entitled, respectively, "Operationalizing the Fiscal Responsibility Framework." and "Reviewing the Fiscal Responsibility Framework.

[32] These included "Towards an Integrated Legal Framework for Public Financial Management, December 2010;" "Developing the Charter for Fiscal Responsibility, April 2015;" "Fiscal Management of Oil Resources, January 2019;" "Advancing the Fiscal and Legal Framework for Petroleum Revenue Management, October 2019."

Box 5. Technical Assistance on Fiscal Rules: The Case of Jamaica

A case study of IMF assistance in the design of fiscal rules that turned out positively is Jamaica in 2010–14. This case also illustrates the evolution of IMF advice in this area.

In 2010 Jamaica adopted a Fiscal Responsibility Framework (FRF) as amendments to existing laws governing public financial management. This required the Minister of Finance to take measures to reduce, by the end of fiscal year 2016: the fiscal balance to zero, the debt/GDP ratio to 100 percent; and public sector wages as a share of GDP to 9 percent. The framework was tightened in 2014 to require the Minister, by the end of 2018, to specify a multiyear fiscal trajectory bringing the debt/GDP ratio down to no more than 60 percent by fiscal year 2026. These numerical rules came with an escape clause to be activated in response to natural disaster, other emergency or severe economic downturn, after verification by the Auditor General.

In May 2010, after a first set of draft amendments had been passed by the Jamaican parliament, FAD provided TA describing measures to strengthen the FRF (IMF, 2010). This document staked out a cautious position on the desirability of numerical rules, noting that these might encourage procyclicality, incentivize low-quality measures, distract from more important reforms, and incentivize creative accounting. It emphasized more generally that their advisability depended on country circumstances. It recommended clarifying definitions, strengthening the independence and capacity of the Auditor General, publishing more comprehensive budgetary information, specifying the contents of the Fiscal Policy Paper providing macroeconomic and fiscal projections, tightening the escape clause, and introducing sanctions for non-compliance.

A 2013 TA report (IMF, 2013a) by FAD then took a more positive position on rules, describing design options and providing detailed recommendations for reforms to strengthen their implementation. It noted the absence from the FRF of clear operational guidance for formulating a medium-term framework, omission of contingent liabilities and off-budget activities, potential for abuse of the escape clause, weaknesses in budget practices such as optimistic revenue forecasts and expenditure overshoots, and recommended further legislative and procedural reforms to correct these defects. After comparing debt, overall balance, expenditure and revenue rules, it recommended a debt rule together with an overall balance rule to anchor fiscal sustainability and provide operational guidance, respectively. It also advocated the establishment of an independent fiscal commission as a medium-term objective. A 2014 TA report (IMF, 2014b) by FAD built on this earlier 2013 document, echoing its recommendations. Following the mission in January 2014, the Government issued a draft act to align the country's legislation with the recommended framework, including only some relatively minor deviations from the IMF's recommendations (pp. 6–7).

The resulting fiscal rules have been pointed to as an example of high-quality design and effective outcomes for other countries to follow (Arslanalp, Eichengreen and Henry, 2024). Moreover, the Independent Fiscal Commission Act was enacted in 2021 and the commission became operational in January 2025.

Sources: IMF (2013a); Arslanalp, Eichengreen and Henry (2024).

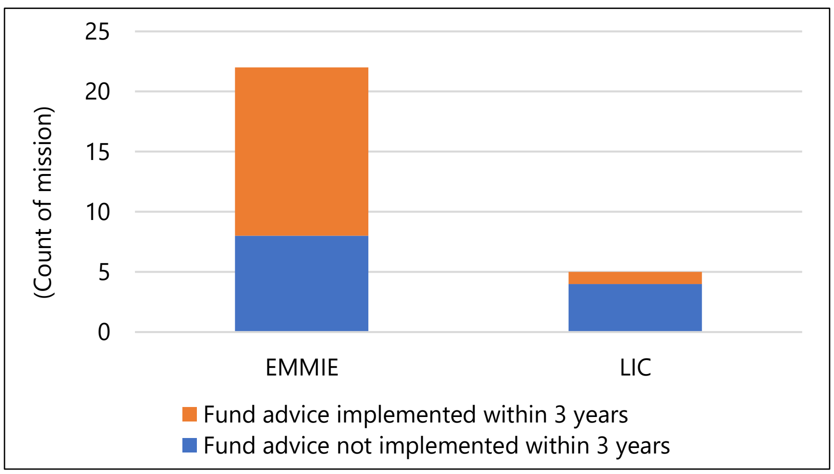
36. **In other countries, TA did not lead to adoption of a fiscal rule.** An example is Sierra Leone, which received four TA reports in 2012–14.[33, 34] Sierre Leone adopted a Public Financial Management Act in 2016 and central government targets for revenue, expenditure, debt and deficits in subsequent years, but these were not embedded in statute or law. Hence, they are not regarded as formal fiscal rules, for instance by the IMF's Fiscal Rule Database, for example.

[33] These included "Public Financial Management- Reform Priorities in the New Fiscal Environment, March 2012;" "Determination and Implementation of a Fiscal Rule, December 2012;" "Improving the Legal Framework for Fiscal Responsibility and Public Financial Management, June 2013;" "Drafting the Public Financial Management Legal Framework, July 2014."

[34] Sierra Leone passed the PFM Act in 2016, and in subsequent years they started setting specific fiscal targets for revenue, expenditure, debt and deficit that the Central Government was expected to meet. https://mof.gov.sl/wp-content/uploads/2023/10/FISCAL-STRATEGY-STATEMENT-FSS.pdf.

37. **In a sample of 27 countries where the Fund provided TA on fiscal rules, nearly 60 percent implemented the advice within three years.**[35] To evaluate the impact of the IMF-provided TA, we analyzed a sample of 27 TA reports published between 2008 and 2023. To identify the reports in which the Fund provided advice on fiscal rules, we first selected a sample based on their title, and then we verified their content. The 27 reports comprised 22 TA missions to EMMIEs and 5 to LICs. We then analyzed whether the recipient country adopted or modified fiscal rules broadly in line with the recommendations formulated in the TA report within three years of its publication. The information regarding the adoption or amendment of fiscal rules was sourced from the IMF's Fiscal Rules Dataset and Article IV reports. The results of the analysis are summarized in Figure 12. Overall, 15 (56 percent) of the analyzed TA missions were followed by either implementation or amendment of fiscal rules. Among EMMIEs, in 14 cases (64 percent) Fund advice was adopted within the 3-year period, whereas for LICs, only 1 mission (20 percent) led to either an implementation or amendment of fiscal rules within three years. In addition, the analysis indicates that some countries implemented the Fund's TA advice with delays, which is not captured in Figure 12. Poland, which was visited by the IMF's TA mission in 2008, implemented the Expenditure Rule in 2012. Guyana, which received TA advice on fiscal rules in 2018, implemented it in 2023.

Figure 12. IMF's TA on Fiscal Rules in a Sample of 28 Countries
(2010=100)



Source: IEO staff calculations.

38. **In a number of cases, TA was provided only subsequent to adoption of a fiscal rule.** An example is India, where the FR was adopted in 2003. Despite repeated violations of the rule, no TA was requested until 2018. This TA report entitled "Reinforcing the Budget as a Main Policy Instrument, July 2018" focused on budgeting processes, with scant attention to fiscal rules. There was no recommendation on how to improve compliance with rules.[36] Another example is Chile, where TA

[35] From the 47 TA reports focusing on fiscal rules, 27 distinct countries were identified. The number of countries is smaller than the total reports because, in some cases, multiple reports pertain to the same country.

[36] Detailed advice was provided only much later in the Article IV report for 2023.

was provided in 2021 ("Fiscal Transparency Evaluation, October 2021") whereas the country's fiscal rules and fiscal council had been established much earlier (in 2001 and 2014, respectively). This suggests that TA sometimes helps to refine the operation of fiscal rules and fiscal councils where they exist, rather than to support their establishment in countries where they are absent.

39. **When examining the timing of TA and implementation of recommendations, we found that the IMF's Fiscal Rules database had somewhat patchy coverage of smaller and/or poorer countries.** At least a few such countries, such as Albania and Ghana, other documentation indicated that there were fiscal rules in place, but these are not listed in the database. Their rules may have been overlooked. Alternatively, it may be that the dataset includes only includes countries with formal, codified rules that meet specific criteria set by the IMF, and that rules in countries such as Albania and Ghana are not regarded as rising to this level.

IV. ASSESSMENT

40. **The IMF has played a prominent important role in the development of literatures on fiscal rules and councils.** Its advice on fiscal rules, institutions and procedures has evolved, mirroring developments in the scholarly literature. Whereas early analytical work at the Fund (Kopits and Symansky, 1998) focused on "a permanent constraint on fiscal policy through simple numerical limits on budgetary aggregates," subsequent advice emphasized the need to balance simplicity, flexibility and enforceability. Recent advice (Caselli and others, 2018; Davoodi and others, 2022c) has highlighted the importance of adjusting budgetary aggregates for the cycle, or else supplementing well-defined debt rules ("fiscal anchors") with a single operational rule focusing on the expenditure side of the budget, thereby introducing a degree of countercyclical flexibility. This emphasis on flexibility mirrors conclusions in the scholarly literature, while the Fund's focus on expenditure rules has played a role on how such flexibility has been enhanced in practice (such as in the case of Europe). Further, the Fund has increasingly emphasized the advantages of supplementing fiscal rules with independent fiscal councils.

41. **By implication, the Fund in its recent advice has done a good job of acknowledging potential costs (in terms of rigidity, complexity, procyclicality, negative investment impacts, creative accounting) as well as potential benefits (in terms of fiscal discipline).** It has described characteristics of well-designed rules that may increase the benefit/cost ratio, labelling rules with these features "second-generation fiscal rules" (Caselli and others, 2018). It has similarly identified the characteristics of fiscal councils most strongly associated with adherence to rules and accuracy of forecasts (Beetsma and others, 2019). In terms of enforceability, the Fund's recent advice has emphasized the need for a strong legal framework in the form of a financial responsibility law, and the role of institutions such as fiscal councils in enhancing budgetary transparency and raising costs of noncompliance. IMF advice has thus kept pace with the scholarly literature.

42. **The Fund has assembled useful databases on fiscal rules and fiscal councils.** These resources have played an important role in enabling in-house and independent analyses of the impact of these institutions. However, these databases have not been updated since 2021.[37] Both the IMF's own analytics and members' learning from peers would be enhanced by up-to-date data and more comprehensive information on institutional aspects of fiscal management. It would be important to check for gaps in coverage, specifically of relatively small and/or poor countries, and to clarify the precise criteria used to categorize countries as possessing or lacking fiscal rules and councils. Annual updating should be routine; doing so would be straightforward with the cooperation of Area Departments. Below we recommend that attention to fiscal rules and fiscal institutions should be an obligatory component of Article IV missions. This would make addition of up-to-date information to the database even more straightforward.

43. **The IMF has engaged with member countries extensively in the area of fiscal rules, as part of both its surveillance and TA activities.** TA on fiscal rules and procedures is extended much less frequently to LICs than EMEs, however. It may be that officials in LICs, who request such assistance, are of the view that fiscal rules are difficult to enforce and that independent fiscal councils are difficult to staff in their setting. Another factor may be that donor funding for TA to LICs is not targeted at this question. It is important to ask whether this imbalance should be rectified.

44. **In some countries, TA has led to the adoption of new fiscal rules and improvements in the design of existing fiscal rules and frameworks.** In other cases, however, even repeated TA did not lead to adoption of fiscal rules. In a number of countries, TA was provided only subsequent to adoption of a fiscal rule. In fact, it appears that TA in some cases tends to be oriented toward refining the operation of fiscal rules and fiscal councils where they exist, rather than establishing them where they do not.

45. **Fiscal rules and procedures are covered frequently in Article IV reports, but coverage is uneven.** The IMF has shifted over time from a relatively heavy focus on fiscal rules in AEs in its Article IV reports to a heavier focus on EMs. Fiscal rules continue to receive relatively little attention in Article IVs for LICs. A significant number of Article IV reports for LICs make no mention of fiscal rules and procedures. It could be that staff is of the view that fiscal rules are only effective where there exists a political commitment to enforce them and that such commitment is absent in LICs. Or their view could be that fiscal councils are difficult to staff and operate in LICs (smaller LICs in particular), where an adequate supply of independent experts is lacking.[38] Or it could simply be that there is a tendency for staff to pay more attention to the design and impact of fiscal rules and councils where these are already in place.

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[37] An update is now ongoing and should be available by end-2025.

[38] The IMF's own Staff Guidance Note on engagement with small developing states (IMF, 2024a) suggests that inadequate capacity is not uniformly a problem in small economies, writing that small developing countries "can also further strengthen the credibility and transparency of their fiscal frameworks by setting up fiscal councils—where capacity allows—and encouraging independent analysis and forecasts."

Possible Ways Forward

46. **To enhance the relevance and impact of advice on fiscal rules and institution, the Fund could consider the following suggestions:**

47. **Where TA on fiscal rules and institutions has been provided, its recommendations could be routinely incorporated into Article IV reviews.** More generally, the IMF could do more to prepare the ground for the adoption of appropriate fiscal rules, institutions and procedures. Building on the conclusions of TA reports in Article IV consultations is one way of going about this. This approach aligns with the conclusions from the 2024 review of the Fund's Capacity Development (CD) strategy, which stressed the importance of further deepening CD integration with the Fund's surveillance and lending activities (IMF, 2024c).

48. **Consideration of fiscal rules, institutions and procedures (their current state and desirable reforms, if any) could be flagged as an obligatory element of every Article IV report, just as the aggregate fiscal accounts (the debt and deficit as a share of GDP) are an obligatory element of every report.** Staff may conclude that numerical fiscal rules and independent fiscal institutions are inappropriate to country circumstances.[39] Where it would be appropriate to establish fiscal rules and procedures, staff may signal their macro-criticality but defer deeper coverage, e.g., if more time is needed to reconcile pre- and post-COVID era fiscal rules or to improve understanding and conduct empirical studies on how to take into account country-specific context, i.e., political economy, development needs, multiple shocks. But making the question a standard component of Article IV reviews would have the salutary effect of directing the attention of country economists and Article IV missions to the state of rules and institution, which have not always been top of mind. There are many competing calls on staff resources, but the time and effort involved would be limited. The observation that such rules and institutions sometimes remain unchanged for extended periods does not weaken the case. The alternative of delegating the monitoring and updating of fiscal rules and institutions to a dedicated unit in FAD is less appealing. This would have the effect of walling off attention to these issues and encouraging country economists and Article IV teams to assume that they are some else's responsibility. Where fiscal rules and procedures are in place, staff should routinely discuss compliance and violations and analyze how such rules and procedures affected fiscal planning and outcomes.

49. **Staff should make further efforts to tailor advice on fiscal rules and institutions to country circumstances.** A positive example of this is the Fund's proposed framework for fiscal rules in resource rich economies. But resources riches are not the only dimension along which country circumstances differ. More thought could be given to other country characteristics whose presence or absence warrants an adjustment in the content of recommendations.

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[39] For example, LICs and fragile and conflict affected states often do not have the fiscal institutions nor data required for effective fiscal rules.

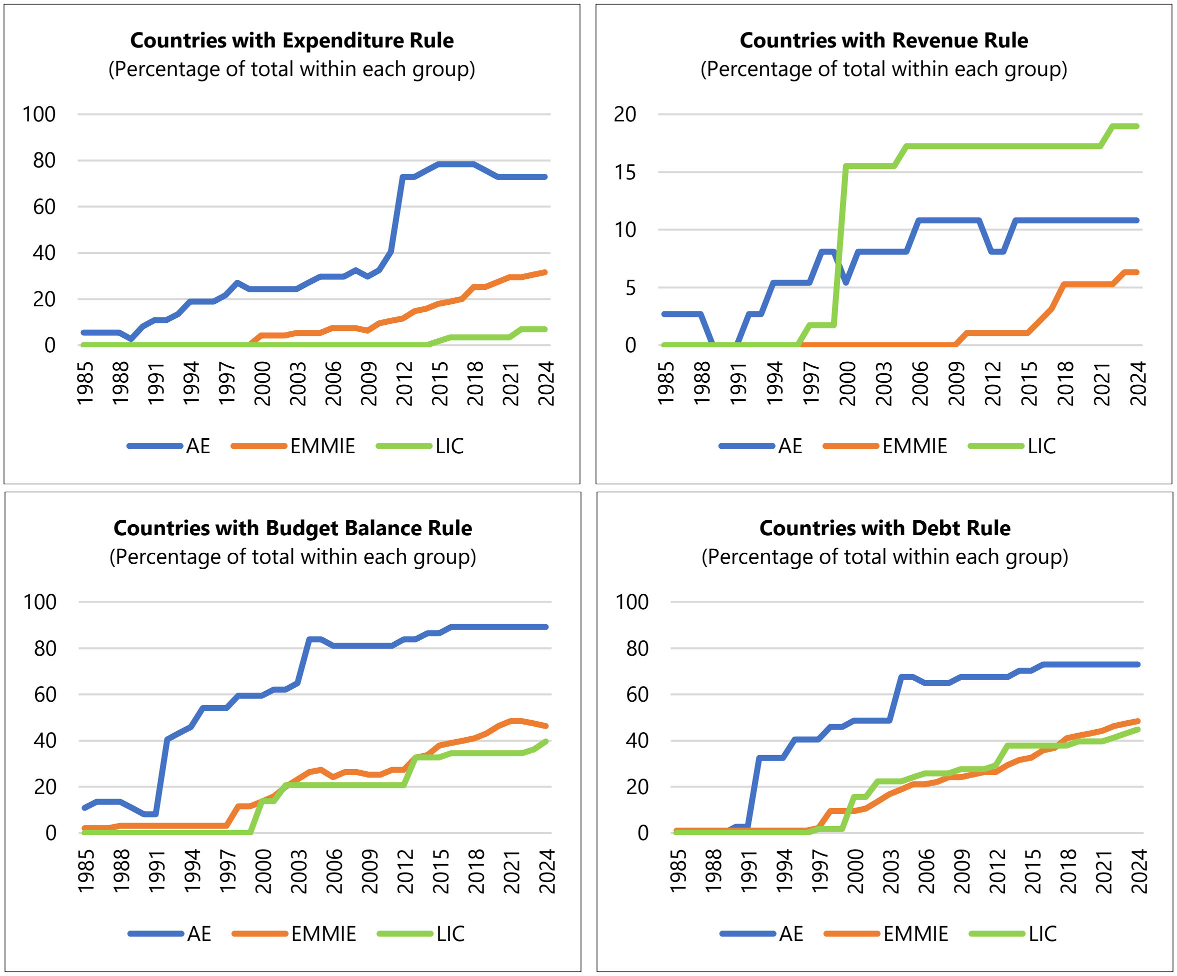
50. **Specifically, staff could do more to articulate appropriate differences in fiscal rules, fiscal councils and related arrangements between countries with high and low institutional capacities.** This is important since the effectiveness of fiscal rules and procedures depends on the broader institutional context. Should countries with relatively low institutional capacity adopt no rules, or relatively simple rules? Should they start with fiscal rules and only subsequently, as their institutional capacity develops, add fiscal councils? At what point is institutional capacity sufficient to proceed from simple to more complex fiscal rules? At what point is it appropriate to supplement the fiscal rule with a fiscal council? These operational specifics, needed to provide concrete guidance to IMF country desks and Article IV missions, have not been addressed in the IMF's analytical reports and flagship reports.

51. **A thorough analysis of compliance with different kinds of fiscal rules in countries with different institutional capacities and different per capita incomes would be key to providing more tailored guidance to countries.** The OECD has done work on compliance with rules in AEs; the IADB has analyzed compliance in 14 Latin American countries. We are not aware of a comprehensive analysis of compliance and its correlates for IMF members.[40] An analysis of compliance with rules could usefully distinguish the economic circumstances under which rules are adhered to versus being violated (in good versus bad times, for example). It could pay attention to the specificities of fragile countries, if relevant. It could distinguish compliance (whether a specified numerical rule is strictly met) from effectiveness, that is, whether the existence of a rule encourages convergence toward that numerical target even if it is not strictly met (as in Caselli and others, 2018). It could undertake these analyses separately for expenditure rules, revenue rules, balanced budget rules and debt rules. It could ask whether fiscal rules are macro-critical. Can one attribute major fiscal problems to their absence, inadequacy or failure?

52. **It would be beneficial for the Fund to undertake a comprehensive examination of the benefits of fiscal councils across diverse country contexts.** We are not aware of systematic analysis of the impact of fiscal councils on budgetary outcomes and forecast accuracy in different country settings (in small versus large countries, in countries with higher and lower institutional capacity, in countries subject to different levels of macroeconomic volatility etc.). Such an analysis would be important for informing staff recommendations regarding the establishment and design of such arrangements in the context of both TA and Article IV reports.

[40] The closest approximation is Caselli and Reynaud (2019), who examine the impact of fiscal rules on fiscal balances using a version of the IMF Fiscal Rules Dataset through 2015 (finding no causal effect). This study does not however consider variations across countries with different structural characteristics.

APPENDIX I. SHARES OF COUNTRIES WITH SPECIFIC FISCAL RULES



Source: IEO staff calculations based on IMF data.

Appendix II. List of Keywords Used in Text Analysis

Figures 5 and 7 – Panel A: Fiscal rule, fiscal rules, fiscal responsibility law, fiscal target, fiscal targets, fiscal indicator, fiscal indicators, fiscal stabilizer, fiscal stabilizers, revenue rule, revenue rules, budget balance rule, budget balance rules, expenditure rule, expenditure rules, debt rule, debt rules, national rule *and* fiscal, national rules *and* fiscal, supranational rule *and* fiscal, supranational rules *and* fiscal.

Figures 5 and 7 – Panel B: Fiscal council, fiscal councils, independent fiscal institution, independent fiscal institutions.

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CHAPTER 3—THE IMF'S ADVICE ON PUBLIC DEBT MANAGEMENT

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

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EXECUTIVE SUMMARY

This chapter assesses the Fund's advice regarding public debt management, understood as the strategies and actions aimed at meeting a government's financing needs and payment obligations at the lowest cost, while minimizing associated risks and supporting policy objectives. It focuses especially on advice to emerging market and middle-income economies (EMMIEs).

The Fund has played a significant role in supporting countries with public debt management challenges through various initiatives—often in collaboration with the World Bank—bilateral and multilateral surveillance, and capacity development (CD). This support has been underpinned by extensive involvement of different departments. The IMF's approach reflects a broad institutional consensus on the importance of both debt sustainability and sound risk management practices.

Key initiatives include the development of comprehensive guidelines on public debt management, a framework for medium-term debt strategies, and efforts to promote and improve debt transparency and fiscal data reporting. The IMF has also conducted relevant research in the area of public debt management. It has paid attention to emerging issues in public debt management, such as the growing importance of new lenders and climate finance.

The IMF has offered relevant guidance on vulnerabilities related to debt profiles and debt management of EMMIEs through both multilateral and bilateral surveillance. The IMF's flagship publications have consistently raised concerns about fiscal risks in EMMIEs and frontier economies with high debt levels, highlighting the vulnerability to the effects of monetary policy normalization in advanced economies.

In bilateral surveillance the Fund has periodically updated its debt sustainability assessment tools, placing greater emphasis on identifying liquidity risks and vulnerabilities linked to debt composition and contingent liabilities. A review of Article IV reports for 12 EMMIEs indicates that IMF staff regularly focus on such vulnerabilities.

The Fund's CD activities in the area of debt management have been intense. Available evidence indicates that these activities are valued by member countries, including EMMIES, and generally well-received by national authorities.

Nonetheless, the Fund's efforts in public debt management are not always fully integrated across its various functions. There is scope to enhance cross-referencing between institutional work (such as the "Guidelines on Public Debt Management" and other analysis conducted by the IMF's functional departments) into the Fund's flagship documents and bilateral surveillance reports. Article IV consultations often focus on "above-the-line" fiscal metrics while devoting less attention to financing strategies and debt vulnerabilities. While interaction between technical assistance (TA) and surveillance does occur in practice, systematically integrating TA with surveillance would strengthen the effectiveness of the Fund's advice on public debt management.

Although the Fund maintains several public debt databases, their coverage, disaggregation, and consistency are inadequate to meet the growing complexity of global debt structures. The rise of nontraditional creditors, novel debt instruments, and opaque bilateral loan agreements poses a serious challenge to the accuracy and utility of current debt data. The Fund could also usefully develop a database with information on Debt Management Offices in member countries.

The IMF and World Bank maintain particularly close coordination on debt-related issues, supported by joint initiatives like the Debt Management Facility and several other joint initiatives. Coordination across IMF departments seems generally effective, supported by a clear division of labor. However, given the many departments involved in Fund's work on debt management, regular assessments of coordination practices would be useful for maintaining consistency and coherence in the Fund's activities in this area.

I. INTRODUCTION

1. **Since the Global Financial Crisis (GFC) and the COVID-19 pandemic, vulnerabilities related to public debt have increased dramatically.** Some Low-Income countries (LICs) and Emerging Markets and Middle-Income economies (EMMIEs) faced sovereign defaults in 2022–23.[1] Higher interest rates have rendered sovereign debt dynamics less favorable (IMF, 2024a). Recent events have pointed up the importance for economic and financial stability of not just the level and trajectory of debt but also its composition (currency denomination, maturity structure, investor base, etc.). They have also highlighted the importance of well-designed institutions for managing these risks.

2. **Vulnerabilities related to debt profile have been on the radar screen of market participants, governments and the IMF since the Mexican and Asian financial crises of the 1990s if not before.**[2] Initiatives have been taken to foster the development of markets in long-term, domestic currency denominated public debt held by a diverse population of institutional investors. Debt sustainability frameworks for market access and low-income countries (LICs) have become a workhorse of IMF surveillance.

3. **The importance of institutionalizing sound practices for debt management has gained particular urgency with the proliferation of financial instruments and additional classes of investors.** The importance of institutions and procedures to ensure debt transparency was lent prominence by the Greek crisis starting in 2009, for example, triggered by revelations of the partial and misleading nature of debt and deficit figures. The participation in debt markets of nontraditional creditors, including official creditors that are not members of the Paris Club, and the advent of liabilities other than standard debt securities, such as loans with covenants featuring nondisclosure clauses, raise further questions about the adequacy of existing statistics on debt flows.

4. **The objective of this chapter is to assess the Fund's advice in the area of public debt management.** This is defined as the strategies and actions to ensure that the government meets its financing needs, payment obligations, and policy objectives at the lowest possible cost, while minimizing risks, including from contingent liabilities.[3] Fund's advice on fiscal policies that affect the size and composition of the overall balance (the so-called "above the line" components of

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[1] Country groupings are consistent with that in other Background Papers to the evaluation (Cohen-Setton and Montiel, 2025; De Lannoy and Lane, 2025; Ocampo and Zoli, 2025). See Appendix to those papers for a full list.

[2] Thus, the Mexican crisis highlighted that relying on nonresident investors and short-term debt indexed to foreign currency exposes a government and country to capital flow reversals (e.g., Frankel and Schmukler, 1996). The Asian crisis then pointed up the risks of foreign currency and short-maturity debt. See Eichengreen and Hausmann (1999) on the first, Chang and Velasco (2000) on the second. The 1990s marked something of a breakpoint for public debt management in emerging markets and, effectively, inaugurated the current era in that it marked a transition from syndicated bank lending to the bond finance characteristic of the present day.

[3] The paper only focuses on the liability side of the public balance sheet; it does not cover the asset side, especially relevant for countries that have sovereign wealth funds.

the fiscal accounts) is not covered here but discussed in Cohen-Setton and Montiel (2025), De Lannoy and Lane (2025), Ocampo and Zoli (2025) for different country groupings. This chapter asks whether the coverage and content of IMF advice on public debt management have been adequate and how these might be improved. The chapter focuses on Fund's advice on debt management in the context of surveillance, though references to capacity development (CD) and program cases are covered when relevant. The chapter asks whether advice regarding public debt management might be better integrated into the Fund's Article IV reports in addition to being provided via technical assistance (TA). It focuses on EMMIEs. Debt issues related to LICs will be fully addressed in future evaluations, although unavoidably they are touched on in this paper. The paper does not cover debt restructuring issues, which are outside the scope of the evaluation (IEO, 2024a).[4]

II. PERSPECTIVES ON PUBLIC DEBT MANAGEMENT

5. **The importance of public debt management issues has long been appreciated inside and outside the IMF, but these issues are now more important than ever.** Debt burdens have soared to unprecedented peacetime heights in the wake of the GFC and COVID-19 pandemic. Figure 1A, based on the IMF's World Economic Outlook data, shows the evolution of general government debt-to-GDP ratios for advanced economies (AEs), EMMIEs, and LICs. Step increases around the time of the GFC and COVID-19 are clear for AEs and EMMIEs, while in LICs debt ratios have increased steadily since 2012. Debt decomposition analysis indicates that the average increase in public debt to GDP ratios was mainly driven by primary deficits in all country groups, whereby the differential between real interest rate and growth has mitigated debt accumulation (Figure 2). In EMMIEs and LICs exchange depreciation and especially other stock-flow adjustments have also been an important driver of debt dynamics.[5]

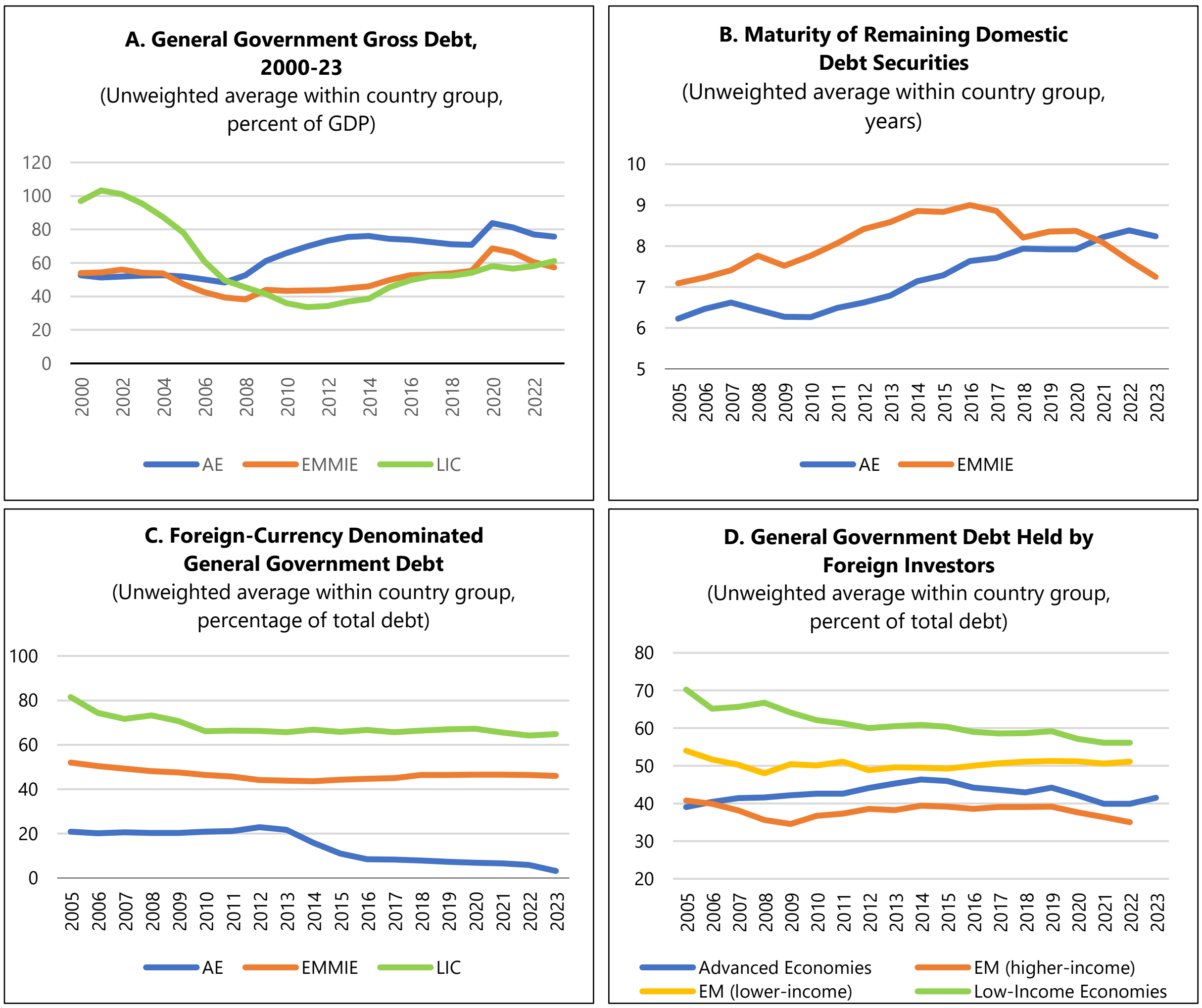
6. **The residual maturity of debt, the share that is foreign currency denominated, and the share held by external investors show the existence of continuing macro-critical risks in LICs and EMMIEs (Figures 1B, 1C, and 1D).** Distributions within country groups point to significant heterogeneity in this respect, with first and third quartile of EMMIEs' residual maturity of domestic government securities at four and nine years in 2023, respectively (see Appendix I). Shares of foreign currency denominated debt also vary, but were very sizable in some economies, with the third quartile as high as nearly 70 percent and 80 percent for EMMIEs and LICs, respectively.

[4] The Fund is involved in various initiatives on debt restructuring, e.g., it co-chairs the Global Sovereign Debt Roundtable aiming to enhance common understanding among stakeholders involved in debt restructuring; it has an important role in Common Framework for debt resolution and was instrumental in the Debt Service Suspension Initiative. The Fund has also produced policy work in this area (e.g., IMF, 2021). Fund's work on debt restructuring will be covered in another ongoing IEO evaluation.

[5] Examples of contingent liabilities that resulted in large fiscal costs in EMMIEs over the evaluation period included Azerbaijan (2010), Hungary (2012), Sebia (2012), and Ukraine (2008–10), Bova and others, (2016). Large government guarantees to SOEs contributed to the increase in public debt in Sri Lanka that ultimately required debt restructuring (See Section VII below, and Annex I).

7. **Management of these debts can be analyzed first through the lens of magnitudes, accompanied by the risks and vulnerabilities they entail.** Observing debt management from this vantage point focuses on the level of debt (which can raise issues of sustainability), its maturity structure (which may give rise to rollover risk), its currency composition (which may be subject to destabilizing exchange rate changes), and the investor base (which may expose debt markets to sudden outflows and associated asset-price changes in instances where that base is dominated by nonresident investors).

Figure 1. Government Debt Levels and Composition



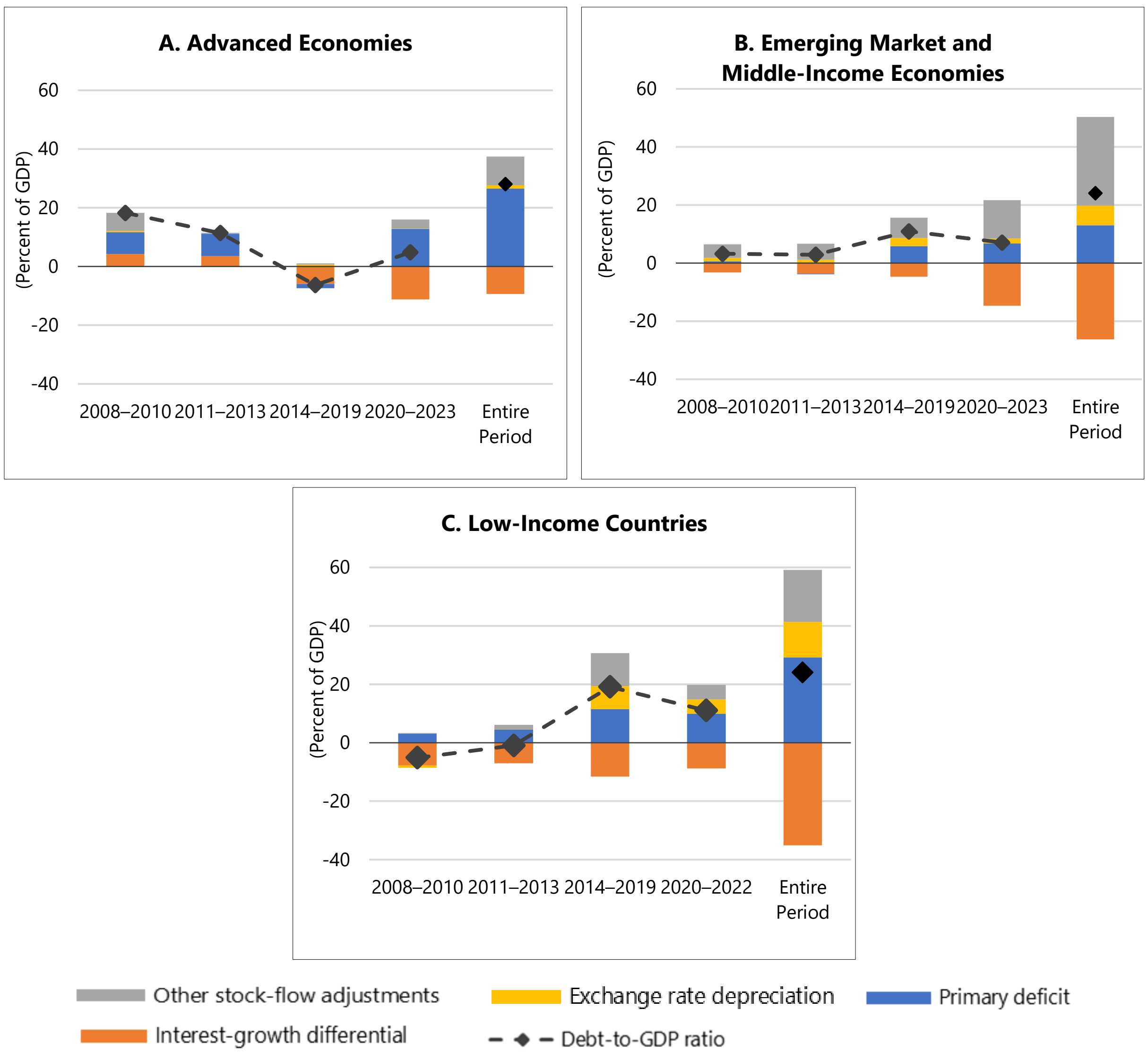
Sources: Arslanalp and Tsuda, 2014; BIS; WEO; IEO staff calculations.
Note: AE = Advanced Economy; EMMIE = Emerging and Middle-Income Economy, LIC = Low-Income Country. Country coverage depends on data availability. Figure 1.B covers 16 AEs and 13 EMMIEs; data for LICs were not available.

8. **Debt management can also be viewed through the lens of institutional arrangements.** This perspective directs attention to where responsibility for debt management is lodged, to the training and expertise of debt managers, and to procedures governing debt management decisions. Issues here include whether there exists a dedicated Debt Management

Office within the finance ministry or central bank or operating independently that is responsible for executing the government's debt management strategy, for assessing the tradeoffs associated with different strategies, and for providing advice to governmental decision makers, or whether these responsibilities are instead spread across different branches and units of government. Issues here also include whether there exist institutional arrangements adequate for assembling a comprehensive picture of the debt (whether the statistical basis for making debt-management decisions is adequate), and whether the resulting picture is transparent (whether statistics are promptly and fully disseminated within government and released to investors and the public).

Figure 2. Decomposition of Public Debt Changes

(Percent of GDP, unweighted average)



Sources: MAC DSA data; IEO staff calculations.

III. FUND'S WORK ON PUBLIC DEBT MANAGEMENT

9. **Fund's work on public debt management has developed in two main directions.** The first is offering guidance for country authorities on how to enhance the institutional framework and practice of debt management as well as on building capacity to conduct debt sustainability analysis; the second involves initiatives to strengthen public debt transparency. The Fund's work in these areas is carried out by multiple departments, often in collaboration with the World Bank, as discussed below.

A. Guidance on How to Enhance the Institutional Framework and Practice of Public Debt Management

10. **The IMF has long collaborated with the World Bank to provide relevant and comprehensive guidelines for public debt management.** These efforts date back to at least 2001, when IMF and World Bank (2001a, b) issued "Guidelines" emphasizing the importance of sound debt management. Issues included coordination with the fiscal and monetary authorities, transparency and accountability, a sound institutional framework, a coherent debt management strategy, a risk management framework, and development of a local market for government securities. An accompanying document (IMF and World Bank, 2003) provided case studies of AEs and EMMIEs focusing on the issue areas highlighted in the main document.

11. **In response to a request from G-20 finance ministers and central bank governors, the two institutions usefully issued revised Guidelines in 2014 (IMF and World Bank, 2014).** The main changes clarified the roles and accountability of debt managers and emphasized their responsibility for providing information to fiscal authorities and communicating with investors. They incorporated the implications of adding collective action clauses to bond contracts, elaborated risk management strategies, attached greater emphasis to stress testing, and highlighted the need to enhance the liquidity of the domestic bond market. The updated Guidelines emphasized that debt managers should operate separately from monetary and fiscal authorities (while coordinating with them). They recommended that debt management functions should be consolidated in a single, clearly identified authority.

12. **At the time of the GFC the IMF and World Bank developed a framework to help country authorities design a medium-term debt management strategy (MTDS).** This framework, created in 2009 and updated in 2019, helps guide government's decisions on the composition of debt (currency of denomination, indexation, maturity) by comparing ex ante and ex post costs of such debt under both baseline and stress scenarios (IMF and World Bank, 2009; 2019a, 2019b).

13. **The Fund produced—again in collaboration with the World Bank—detailed guidelines for developing local currency bond markets (IMF and World Bank, 2016; 2021).** This initiative grew out of recognition that over-reliance on foreign currency borrowing exposed developing countries to higher risk, and that developing local currency markets for public debt would enhance

access to finance for domestic investment. These offer also a useful diagnostic tool to assess the level of market development, discuss challenges faced by EMMIEs and LICs in their market development process, and provide guidance on overcoming them (IMF and World Bank, 2013).

14. **The IMF has also conducted relevant research in the area of public debt management.** In 2010, MCM analyzed the relationship between the management of public debt on the one hand and financial stability on the other, addressing the roles of debt levels, debt composition, the investor base, capital market structure (market liquidity and existence of a well-defined yield curve), and institutional aspects, including coordination with monetary authorities, communication with market participants, adequacy of the legal framework for debt management, and qualifications of staff (Das and others, 2010). Another MCM paper (IMF, 2011a) focused on the implications of financial crises for debt management, considering the adequacy of risk management frameworks and practices and potential negative feedback to the financial and fiscal sectors. It emphasized the importance of liquidity buffers in a crisis-prone environment.

15. **More recently, the Research Department (RES) provided new analysis of the incidence and risks associated with short-term debt in different country groupings (Chen and others, 2019).**[6] The authors found that while the median maturity of government debt is similar across AEs, EMMIEs, and LICs, reliance on short-term debt is greater among EMMIEs and LICs when issuing on local markets. Among these countries, those that have lengthened the maturity of public debt have done so by accepting greater exposure to exchange rate risk, since longer maturity issues tend to be foreign currency denominated. The authors observe that maturities decline in response to crises in all country groupings and recommend building liquidity buffers (reserves of liquid assets). They point to the importance of addressing data gaps regarding debt maturity, specifically in LICS and EMMIEs where financial accounts and flow of funds data are incomplete.

16. **The Fund has worked also on more cutting-edge approaches to debt management, such as the Sovereign Asset and Liability Management (SALM) approach.** This method focuses on the consolidated public sector balance sheet, including contingent liabilities (Udaibir and others, 2012; IMF, 2014a; Amante and others, 2019).[7] It aims at mitigating vulnerabilities related to both assets and debt—through a comprehensive, integrated approach—by measuring how changes in economic and financial indicators—such as exchange rates, interest rates, inflation, and commodity prices—affect sovereign assets and liabilities. Applying this framework presents significant challenges, as it requires clearly defined macroeconomic and SALM objectives, accurate projections of future public revenues, and a comprehensive evaluation of both on- and off-balance sheet liabilities. Furthermore, effective coordination among relevant public entities is essential for its successful implementation.

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[6] This paper was written in response to a request from the IMF Economic Counsellor and Director of the Research Department.

[7] The Fund has also developed the Public Sector Balance Sheet (PSBS) Database, which shows comprehensive estimates of public sector assets and liabilities that formed the basis for the analysis presented in the October 2018 edition of the Fiscal Monitor (IMF, 2018a).

B. Fund's Initiatives to Enhance Public Debt Transparency[8]

17. **The Fund has launched in collaboration with the World Bank initiatives to address cases of sizable hidden debts.** In two joint notes the IMF and World Bank discussed: (i) how TA can assist low and lower-middle-income countries in building capacity in public debt recording, monitoring, and reporting; and (ii) their own role in data collection, dissemination, and analysis, as well as in the formulation of debt data reporting standards and guidelines (IMF and World Bank, 2018a).

18. **The Fund has also developed a Fiscal Transparency Code and conducted Fiscal Transparency Evaluations.** The Code—approved by the IMF Board in 2014—is the international standard for disclosure of information about public finances (IMF, 2014b). A Fiscal Transparency Handbook (IMF, 2018b) provides guidance on the implementation of the Code's principles and practices. Fiscal Transparency Evaluations are assessments of member countries' fiscal transparency practices against the standards set by the Code. They have been published for 36 countries (9 AEs, 20 AEs, and 7 LICs) between 2014 and October 2024.

19. **In 2018 the IMF, jointly with the World Bank, introduced a comprehensive framework to address debt vulnerabilities—the "Multipronged Approach"" (MPA) (IMF, 2020a).** The MPA focuses on: (i) working with members and creditors to produce better debt data; (ii) supporting capacity development in public debt management; (iii) providing tools for analyzing public debt developments and risks, including the IMF's framework for assessing debt sustainability; and (iv) strengthening policies to support transparent and rapid debt resolution. Relevant work in this context includes policy papers on collateralized borrowing (IMF and World Bank, 2020; 2023). Progress under the MPA was assessed in IMF (2023a), which focused on the data-and-transparency aspect of the MPA, somewhat to the neglect of other components. Comparing AEs with EMMIEs and LICs, the report found wider data gaps for the latter, reflecting a larger share of non-marketable debt, greater importance of SOEs, and less developed accounting and reporting practices. On the side of the creditors, the report pointed to the role of confidentiality clause in non-marketable loan contracts as limiting transparency.[9] It concluded that progress had been made under the MPA but that building on achievements would require both institutions to allocate significant additional resources to these initiatives.

20. **The IMF maintains several databases on public debt, but these differ in terms of coverage and reporting methodologies, potentially leading to inconsistencies (IMF, 2023b).** Overall, no single database offers comprehensive public debt data for all countries with the desired disaggregation by instrument, maturity, and creditor classification. Of the 11

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[8] The Fund has also developed tools to analyze and manage fiscal risks, including contingent liabilities, off-balance sheet items, state-owned enterprises, and public-private partnerships (see Cohen-Setton, Montiel, and Zoli, 2025). The Fund also has a debt limit policy requiring disclosure of debt holder profiles for countries under Fund arrangements.

[9] Scholarly analyses (Gelpern and others, 2022) point to specific creditor countries as a source of these troublesome confidentiality clauses, though IMF (2023a) does not name names.

databases on public debt that the IMF maintains alone or in collaboration with other international financial institutions, some focus on government debt (e.g., the Quarterly Public Sector Debt and the Global Debt Database), or have specific series for government debt (e.g., Government Finance Statistics and International Financial Statistics). Others provide partial information on debt, such as the Coordinated Portfolio Investment Survey (which includes data on bilateral cross-country exposures for portfolio securities but does not cover loans or domestic debt) and the Monetary and Financial Statistics (covering debt held by domestic financial sector).

21. **One of the most comprehensive databases is the IMF's Global Debt Database, though this does not offer a breakdown on government debt composition.** It provides total gross debt of the (private and public) nonfinancial sector for 190 countries, in some cases dating back to 1950. On the side of public debt, it distinguishes central government debt, general government debt, nonfinancial sector public debt, and total public sector debt. However, it does not disaggregate debt by currency, maturity, debt instrument, or creditor class; it does not always capture certain debt instruments, such as guarantee schemes; it also does not include the public sector's assets, which are important for distinguishing net from gross debt. Another fairly comprehensive public debt database is the Quarterly Public Sector Debt Database, jointly developed by the IMF and World Bank, which provides broad debt composition by currency (domestic vs. foreign currency), residence of the creditor (domestic vs. external), maturity (short-term vs. long term), and by main instruments at quarterly frequency. However, this dataset does not include a decomposition by creditor type and coverage of debt instruments is patchy.

22. **Additional data are provided by countries voluntarily subscribing to the Fund's Special Data Dissemination Standard (SDDS) and General Data Dissemination Standard (GDDS).** For example, the SDDS, to which 48 countries subscribe at the time of writing, distinguishes short-term and long-term debt, and breaks these down into securities, loans, financial derivatives and other accounts payable. It distinguishes also non-central government debt guaranteed by the central government.

23. **The accuracy and comprehensiveness of the data reported to and disseminated via these vehicles require continuous critical scrutiny.** For example, the participation in debt markets of nontraditional creditors, including official creditors that are not members of the Paris Club, and the advent of new liabilities other than standard debt securities, such as loans with covenants featuring nondisclosure clauses, raise questions about the adequacy of existing statistics on bilateral official debt flows.

C. Institutional Set-Up for Fund's Work on Public Debt Management

24. **The Fund's debt management work is undertaken by multiple departments:**

(i) **Fiscal Affairs Department (FAD):** Specific aspects of debt management are covered by two Public Financial Management Divisions (FADM1 and FADM2), with different regional responsibilities. They focus on (i) the institutional set up for debt management (organizational setting, legal framework, and procedures surrounding the debt management function); (ii) integration of debt and cash management; (iii) fiscal risk management (identification, analysis, mitigation, and disclosure of risks, including contingent liabilities from SOEs, subnational governments, and public-private partnerships); and (iv) accounting and reporting on public sector debt. They maintain a Fiscal Risk Toolkit and work on fiscal transparency initiatives to identify gaps in the reporting of public sector liabilities. They provide TA to country authorities and support area departments, including by reviewing documents for Fund-supported programs and surveillance consultations.

(ii) **Monetary and Capital Market Department (MCM):** The Debt Capital Markets Division (DM) of MCM provides TA and capacity building support on sovereign debt management and market development. It produces policy and analytical work in these areas (e.g., the Guidelines for Public Debt Management, the MTDS framework and the Sovereign Asset and Liability Management work discussed above) and supports the application of debt management policies in country cases, including by reviewing relevant aspects of documents for Fund-supported programs and surveillance consultations.

(iii) **Strategy, Policy, and Review Department (SPR):** The Debt Policy Division of SPR is responsible for design and implementation of Fund policies related to debt sustainability and debt conditionality. It is responsible for creating and maintaining the Debt Sustainability Analysis (DSA) framework (see Section V) as well as building capacity on performing DSAs, both internally, involving IMF staff, and externally, involving government officials. The Debt Policy Division reviews the DSA of about 140 countries (all program cases, high risk countries, and systemic countries), while the DSA of the remaining member countries is reviewed by other SPR divisions. The division also conducts two internal trainings and 8-10 external training per calendar year, in coordination with ICD and the World Bank (on LIC DSAs).

(iv) **Area Departments (ADs):** County teams carry out bilateral surveillance and are the point of contact for TA requests and help identify TA needs in the area of debt management. They cover debt issues, including the DSA, and related policy advice in surveillance and program documents, which are finalized through the Fund interdepartmental review process. Country teams are responsible for incorporating TA advice in surveillance and program documents, as relevant.

(v) **Legal Department (LEG), Statistical Department (STA):** These departments address legal aspects and data issues related to public debt, respectively.

(vi) **Institute for Capacity Development (ICD):** ICD provides training on some aspects related to debt management.

(vii) **Interdepartmental Working Group:** Finally, there is an interdepartmental working group, which convenes periodically to discuss debt issues with the World Bank.

25. **This, clearly, is a relatively decentralized and multifaceted approach to providing input on debt management issues, one that requires close coordination among stakeholders.** For CD, which is largely financed through the Debt Management Facility (Section VII), coordination is done mainly through regular meetings among representatives from FAD, MCM, SPR, and the World Bank.[10] TA missions in the area of debt management are often joint, with staff from FAD, MCM, and the World Bank. A memorandum of understanding between FAD and MCM defines respective areas of responsibility. For surveillance and programs, coordination among Fund departments on debt management issues is primarily through the review process. The final sign-off—explicit or implicit confirmation that debt-management issues have been adequately addressed—rests with the area department on the receiving end of these reviews and SPR. A question is whether this relatively decentralized approach is ideal, or whether the Fund's focus on debt management issues would be sharpened by the creation of a single division possessing expertise in economic, financial, legal and statistical aspects of debt management that would be a single interlocutor for area departments responsible for surveillance and programs.

IV. PUBLIC DEBT MANAGEMENT ADVICE IN FUND'S FLAGSHIPS

26. **References to public debt management-related terms are infrequent in Fund's flagship publications (the World Economic Outlook (WEO), the Global Financial Stability Report (GFSR), and the Fiscal Monitor (FM)).** Neither the guidelines documents nor debt management-related working papers appear to be much mentioned, suggesting that the various workstreams remain somewhat disconnected. There was an uptick in discussion and mentions of public debt management in 2010–12 in the FM and to a lesser extent the GFSR, coincident with increases in debt ratios in the wake of the GFC and debt crisis in Greece. This increase was not sustained subsequently, however (Figure 3). There were no references in these documents in the review period to the IMF/World Bank "Guidelines" of which we are aware, aside from one reference in the April 2006 GFSR.

27. **To better assess the attention devoted to debt vulnerabilities and associated debt management advice in the IMF flagship publications, the rest of the section reviews their content over 2008–23, distinguishing three phases**. The review focuses on Fund's analysis of vulnerabilities arising from debt profile, Fund's advice on how to manage the associated risks, and the institutional set up for debt management and deficit financing. This section does not cover Fund's advice of fiscal stance and its implications for debt level, which are typically discussed in the WEO and FM and are reviewed separately in Ocampo and Zoli (2025) and IEO (2025).

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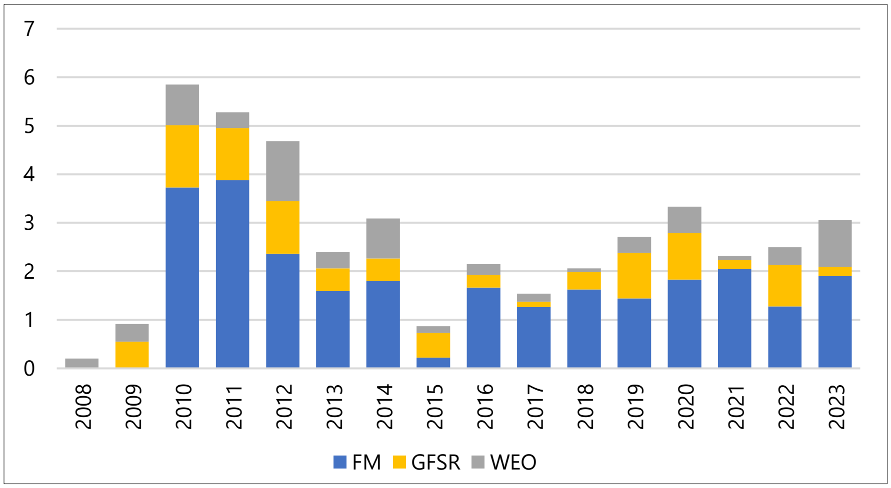
[10] Monthly meetings are typically attended by representatives of FAD, ICD, MCM, SPR, and the World Bank to discuss TA needs in the area of debt management to be financed by the Debt Management Facility In addition, annual steering committee meetings are held annually to discuss the operational strategy for the coming year. The World Bank runs an annual conference, the Debt Management Stakeholders' Forum that is attended by IMF, CD recipients and donors. Steering committee meetings are typically attended by the relevant department representatives at the deputy director levels. Monthly meetings are typically attended by representatives at the A15-B3 levels.

Figure 3. References to Public Debt Management, Flagship Reports
(Proportionate to total number of paragraphs within flagship)



Source: IEO staff calculations.
Note: The list of keywords used in text analysis is reported in the Appendix II.

A. The Global Financial Crisis and the European Sovereign Debt Crisis, 2008–12

28. **In the aftermath of the GFC the Fund drew attention to debt management practices that could help mitigate sovereign financing risks.** A 2011 Board paper (IMF, 2011a) reviewed the sovereign debt management response during 2008–10 in AEs and large EMMIEs and discussed the main lessons for country authorities in managing sovereign debt going forward. When sovereign financing risks sharpened in Europe, both the April 2011 FM and GFSR indicated that debt management offices needed to devise credible funding strategies to limit refinancing risk, by lengthening maturities, actively managing cash flows to smooth bond maturities, and developing a sufficiently diversified investor base.[11]

B. Increasing Debt Vulnerabilities before the Pandemic, 2013–19

29. **As the "taper tantrum" episode highlighted the risks of volatile capital flows, the GFSR warned about possible refinancing challenges for EMMIEs from impending monetary policy normalization in AEs and offered advice to mitigate them.[12]** In addition to other policy

[11] The flagships also focused on policies recommendations for debt reduction. An October 2012 WEO chapter reviewed historical episodes of debt reduction in AEs. The September 2011 FM noted that one-third of LICs were in debt distress or facing high sustainability risks due to long-standing fiscal challenges and high commodity prices and advised to implement measures to boost potential growth (see Cohen-Setton and Montiel, 2025; De Lannoy and Lane, 2025; Ocampo and Zoli, 2025).

[12] The "taper tantrum" refers to the period in the spring-summer 2013 when EMMIEs experienced large capital outflows, triggered by the Federal Reserve Chairman's testimony to Congress about the potential reduction of the Fed's bond-buying program. Marker volatility was particularly severe for countries with larger current account deficits and weaker fiscal positions (e.g., Brazil, India, Indonesia, South Africa, and Türkiye—the so-called "fragile five" at that time).

recommendations to address capital outflows, the October 2013 GFSR suggested debt management operations, such as "using cash balances, reducing the supply of long-term debt, and performing switching auctions to temporarily reduce supply on the long-end of yield curves." It emphasized emerging risks from the unwinding of unconventional monetary policies especially for EMMIEs and LICs that in the previous 10 years had issued bonds internationally for the first time or had reentered the market after a long pause. It highlighted that in some instances this hard currency bond issuance represented a significant increase in external indebtedness and stressed that the unwinding of unconventional monetary policies and eventual rise in interest rates could pose refinancing challenges. It recommended that these countries access international markets only in the context of a comprehensive MTDS, which would identify cost and risk implications. It also advised them to deepen local markets to reduce dependence on volatile foreign capital.

30. **The GFSR also proactively flagged that the recent increase in foreign investor participation in EMMIEs' local government bond markets heightened refinancing risks.** The April 2014 GFSR showed that several sovereigns in this country group had shifted from issuing hard currency external debt to larger presence of nonresidents in local markets. Despite the benefits from financial deepening, this shift also created risks from potential instability in debt portfolio flows. Hence, this type of participation needed to be monitored carefully and accompanied by a deepening of the local investor base, in line with IMF and World Bank (2016), as well as sound macroeconomic policies and better institutions. A similar message was reiterated in the April 2015 and October 2018 GFSR.

31. **The IMF became more vocal and candid also about debt vulnerabilities and refining risks in Frontier Markets[13] and LICs with exposure in international debt markets.** The October 2017 and April 2018 GFSR emphasized the increased vulnerability of these countries to AE's monetary policy normalization, stressing that recent changes in the composition of creditors and debt instruments amplified refinancing risk. The GFSR advised them to strengthen the institutional capacity to deal with risks from the issuance of marketable securities, including through the formulation of comprehensive MTDS, and to explore liability management operations to mitigate refinancing risk. The October 2018 GFSR explicitly identified the frontier markets with large hard-currency bond redemptions in the following five years compared with their reserve buffers, namely: Ecuador, Pakistan, Sri Lanka, and Zambia.

32. **The October 2018 GFSR reiterated that in the EMMIEs with more established financial markets the higher share of foreign nonbank investors in sovereign debt markets made them potentially more vulnerable to external shocks.** It advised policymakers to develop local bond markets and promote a stable local investor base, in line with IMF and World Bank (2016). The GFSR further highlighted vulnerabilities in frontier markets and more

[13] Frontier markets are economies in the in earlier stages of development compared to more established emerging markets. The Fund does not have an official list of frontier economies. The GFSR typically classifies as frontier economies those included in the JPMorgan Next Generation Index and LICs with outstanding Eurobonds.

established emerging markets in a dedicated chapter in October 2019. Both, the October 2019 GFSR and the April 2020 FM, stressed the need to enhance debt transparency in EMMIEs and LICs, encouraging them to publish regular debt reports, broaden the coverage of debt statistics, and provide more detailed disclosure of fiscal spending and guarantees related to SOEs.

C. Pandemic and Post-Pandemic Period, 2020–23

33. **At the onset of the pandemic, the Fund provided quite specific debt management advice to EMMIEs.** The April 2020 GFSR stressed that EMMIEs and especially many frontier market economies were vulnerable to shift in foreign investor sentiment in the context of heightened volatility and higher nonresident participation in debt markets. It alerted sovereign debt managers to prepare for long-term external funding disruptions and emphasized that lowering rollover risks had to "take priority over concerns about containing costs." It recommended to "consider the interactions between the government's financing strategy and other domestic issuers in times of stress to ensure that debt management activities of the government [did] not exacerbate risks." Subsequent GFSR editions continued to highlight risks for EMMIEs and especially frontier market economies with elevated debt vulnerabilities. During the pandemic the Fund also produced a note to advise members on debt management responses (IMF, 2020b), covering not only advice on how to address short-term liquidity and financing needs, but also on monitoring of contingent liabilities.

34. **In the aftermath of the pandemic, the flagships underscored the further rise in refinancing risks and explicitly acknowledged that debt restructuring might become necessary in some cases.** The October 2021 FM highlighted the importance of strengthening the credibility of public finances. The October 2022 GFSR then emphasized that conditions in local currency bond markets had worsened considerably in some EMMIEs and frontier markets, driven by a combination of tightening in global financial conditions, deterioration of fiscal positions since the pandemic, and high exposure to commodity price volatility. It recognized that many frontier markets were facing potential loss of market access and a high probability of sovereign default. It concluded that credible medium-term fiscal consolidation plans were crucial to lower domestic refinancing costs and restore access to international markets. After the sovereign debt default of some frontier markets in 2022, amid tighter global credit conditions, and with a large share of LICs facing high risk of debt distress, the April 2023 GFSR encouraged countries to contain risks associated with their elevated debt vulnerabilities, including through early contact with creditors, multilateral cooperation, and support from the international community. Also, the April 2023 WEO advocated for efforts to address sovereign debt vulnerabilities, including through debt restructuring (IMF, 2023c).[14]

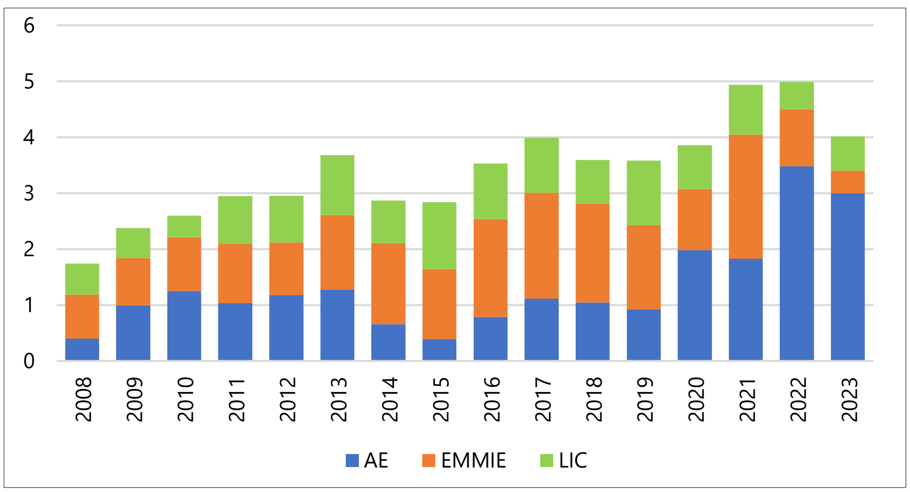
[14] The Fund has also highlighted the growing relevance of private sector debt spillovers and interlinkages with public debt, and the challenges this entails for public debt management (see, for example, Adrian, Qureshi and Tsuruga, 2025).

V. Public Debt Management Advice in Bilateral Surveillance

35. **A discussion of risks from debt composition or debt management policies is not strictly required in Article IV consultations but should be included when relevant.** The 2022 Guidance Note for Surveillance under Article IV consultations lists the following among the elements that "could be considered, where relevant" for the assessment of public finances: "sovereign assets and liabilities, including identifying and mitigating sovereign risk exposures;" "financing needs and financing sources, and possible economic and financial implications;" and fiscal sustainability (IMF, 2022a).

36. **The frequency of mentions of terms related to public debt management, broadly defined, in Article IV reports is fairly even across AEs and EMMIEs (Figure 4).** On the other hand, there is less reference in Article IV reports on LICs. In particular, in the most recent years (2022–23), references to debt management issues are disproportionately found in AEs Article IVs. This increase is mainly related to adoption of the Fund's Sovereign Risk and Debt Sustainability Framework for Market Access Countries in 2021 (see below).

Figure 4. References to Public Debt Management, Article IV Reports
(Proportionate to total number of paragraphs in Article IV reports for country group)



Source: IEO staff calculations.
Note: The list of keywords used in text analysis is reported in the Appendix II.

37. **In Article IV consultations, discussion of debt related issues is anchored to the framework and results of DSA.**[15] The IMF uses different sustainability analysis frameworks for market access countries (MACs) and for LICs.[16] These frameworks have evolved over time to include different modules (IMF 2022b; IMF and World Bank 2018b, 2024). The following section examines key developments in DSA frameworks that are particularly relevant to this paper's focus—specifically, their treatment of vulnerabilities from debt structure and creditor compositions, rollover risks, and risks arising from contingent liabilities.[17] The following section also evaluates the analysis of these aspects, and the associated debt management related policy recommendations, in a sample of recent Article IV staff reports for EMMIEs.

A. Analysis of Debt Vulnerabilities and Debt Management Advice in Article IV Consultations

The Debt Sustainability Framework for Market Access Countries

38. **The framework has evolved from focusing on only solvency to also taking into account liquidity risks, analyzing debt profile and creditor composition, and better capturing contingent liability**

- **Debt Sustainability Assessment for Market Access Countries (MAC DSA) Framework, 2002–12.**[18] This initial variant was relatively simple and focused on sustainability only. It presented projections of the debt-to-GDP ratio over a five-year horizon under a baseline and alternative shock scenarios. No debt composition nor maturity profile indicators were included (IMF, 2002).

- **MAC DSA Framework, 2013–20 Framework.** With this revision, the Fund introduced a definition of public debt sustainability including both solvency and liquidity requirements (IMF, 2011b; 2013),[19] and moved to a risk-based approach through a distinction between

[15] However, staff reports may cover additional debt related issues and vulnerabilities which are not part of the standard debt sustainability framework when important.

[16] For market access countries, the DSA is produced by the IMF, while for LICs, it is jointly prepared by the IMF and the World Bank. The analysis is conducted annually in the context of the Article IV consultations, and more frequently for countries with IMF supported programs. DSAs are drafted by country teams and then reviewed by SPR. Ultimately, there are two "signoffs," one by SPR and one by the area department. In addition, MCM and FAD review draft Article IV reports and may flag debt management-related problems to the relevant area department. They also provide comments and inputs into Selected Issues Papers attached to those reports.

[17] A comprehensive discussion of the DSA frameworks used by the IMF, including of the tools assessing the realism of debt projections, is presented in Cohen-Setton, Montiel, and Zoli (2025). A discussion of realism of debt projections in EMMIEs is provided another background paper to this evaluation (Ocampo and Zoli, 2025).

[18] The framework, first introduced in 2002, was refined in 2003 and 2005 (IMF, 2002; 2003; 2005).

[19] "In general terms, public debt can be regarded as sustainable when the primary balance needed to at least stabilize debt under both the baseline and realistic shock scenarios is economically and politically feasible, such that the level of debt is consistent with an acceptably low rollover risk and with preserving potential growth at a satisfactory level" (IMF 2013, p. 4).

higher and lower scrutiny countries. Analysis of the former entailed additional requirements, including an analysis of the potential impact of contingent liabilities and risks from the debt profile. These were gauged by comparing a set of indicators (e.g., debt held by nonresidents, debt in foreign currencies) to early warning benchmarks derived from a signal approach.

- **Sovereign Risk and Debt Sustainability Framework for Market Access Countries (MAC-SRDSF) Framework, 2021.** The 2021 review of the MAC DSA led to another substantial overhaul of the framework (IMF, 2021b). The new tool, rolled out in late 2022, comprises several modules (Box 1), including one to assess liquidity risk at a medium-term horizon, focusing on the creditor composition and debt structure.[20] Moreover, a realism of financing terms scrutinizes assumptions on new private borrowing and financing terms. The framework also requires countries with narrow coverage of central government debt to conduct a contingency-liability stress-test to capture omitted risk exposure.[21] The SRDSF marks a significant advance in the analysis of liquidity and solvency, though issues remain, most notably the stability of the logit model used to assess the probability of sovereign distress (Box 1).

Box 1. Sovereign Risk and Debt Sustainability Framework for Market Access Countries

The Sovereign Risk and Debt Sustainability Framework (SRDSF) significantly expanded prior coverage and analysis of the debt outlook and vulnerabilities. Compared to previous frameworks, it provides for broader and more consistent debt coverage, longer projection horizons, analytical methods seeking to account for countries' structural characteristics, and stress tests modeling country specific risks (natural disasters, commodity price shocks, banking stress etc.).

Near-term analysis relies on a multivariate logit model, on whose basis countries are classified into high, low/moderate, or low risk of debt distress.[1] For the medium term, the framework relies on a debt fan chart (under alternative macroeconomic and financial assumptions); a gross financing needs analysis (analyzing how large the demand for additional financing may be under adverse scenarios and whether potential financing sources, typically domestic banks, have the capacity to meet that demand); and stress tests for country-specific vulnerabilities. The longer-term framework accounts for demographic developments, changes in natural resources extraction, large debt amortizations, and the fiscal implications of climate change.

The tool provides multiple outputs: (i) A page or more summarizing the debt situation (the trajectory of the debt, future financing needs, a capsule evaluation of the authorities' debt management strategy, and risks associated with the profile of the debt); (ii) A breakdown of public debt and debt service by creditor; (iii) A summary assessment of the risk of sovereign stress; (iv) Five indicators of the structure of the debt (currency composition, maturity investor base, governing law, marketable vs. nonmarketable); (v) A baseline scenario for the medium-term (5 to 10 year) evolution of the debt, accompanied by a fan chart, stress scenario and bound tests (sensitivity analyses); (vi) A long-term risk analysis that projects total public debt and gross financing needs relative to GDP three to four decades into the future.

[1] The logit model considers five "buckets" of variables: an institutional quality measure (from the Worldwide Governance Indicators project), whether the country has a history of debt distress, a set of cyclical indicators, four measures of the magnitude of the debt, and a measure of global risk appetite (the change in the VIX).

[20] The module analyzes how large the demand for additional financing might be in the event of shocks and whether residual financing sources would have space to increase their government exposure. Results of the analysis are summarized in an index measuring the extent to which gross financing needs can be financed over the medium term. Based on the value of this index, risks are categorized either as high, or moderate, or low (IMF, 2022b).

[21] The contingent liability stress-test is also applied to countries with broader coverage of government debt (e.g., general government debt), in case of fiscal risk exposures beyond the chosen coverage (e.g., when guarantees on other entities' debt, such as SOEs, are relevant).

The Debt Sustainability Framework for LICs (LIC-DSF)[22]

39. **The LIC-DSF is used for LICs as well as for the subset of EMMIEs, classified as Small Developing States, that are eligible for concessional lending.**[23] This framework has been revised periodically since its introduction in 2005 (IMF and World Bank, 2005). The latest major revision was in 2018. Supplemental changes were introduced in August 2024 (IMF and World Bank, 2018b; 2024), and a comprehensive review is currently underway The 2018 framework combines indicative rules and staff judgment to assign risk ratings of external debt distress. Countries are divided into three categories according to the value of a Composite Indicator of debt carrying capacity (Strong, Medium, and Weak), which is a function of macroeconomic and institutional variables. Thresholds for prudent debt and debt service ratios (e.g., external debt to GDP and external debt service to exports) are specified separately for each of the three country categories. The 2024 revision of the LIC-DSF puts more emphasis on domestic public debt vulnerabilities and the consistency of the domestic public borrowing plan with maintaining macroeconomic and financial stability. Scenarios are subjected to standard stress tests and in some cases tailored stress tests, including realization of contingent liabilities from SOEs, and market-financing shocks where market access exists. Coverage of the relevant magnitudes is comprehensive, but there are also gaps in data coverage and analysis, for example regarding the identity of external private creditors (e.g., whether these are hedge funds or institutional investors) and the identity of external official creditors (whether they are members of the Paris Club or not).

Analysis of Debt Vulnerabilities and Advice on Debt Management in a Sample of Article IV Staff Reports

40. **To assess the discussion of debt vulnerabilities from debt profile and the advice on debt management in bilateral surveillance, we reviewed the staff reports of 12 Article IV consultations in EMMIEs, conducted in 2022 or 2023.**[24] The sample covers countries with a government debt to GDP ratio above 70 percent as we sought to ascertain whether a discussion of debt vulnerabilities and debt management policies was present for countries with elevated debt obligations.

41. **In 10 of the 12 staff reports, the annex on debt sustainability clearly discussed implications for debt risks of debt profiles and gross financing needs.** The write-ups highlighted factors, such as investor base, maturity structure, currency composition of debt, as well as other elements (e.g. contingent liabilities, arrears), that exacerbated or mitigated risks. There was some variability in how results from the DSA annex were referenced in the main text of

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[22] A more detailed analysis of the LIC DSF is von Luckner (2024), and Cohen-Setton, Montiel, and Zoli (2025).

[23] Of the 97 countries categorized as EMMIEs, 11 use the LIC-DSF framework.

[24] The sample comprised the following staff reports for the Article IV consultations: Angola (2023), Antigua and Barbuda (2023), Bahamas (2023), Bolivia (2022), Brazil (2023), Dominica (2023), El Salvador (2023), Jamaica (2022), India (2023), South Africa (2023), St. Lucia (2023), St Vincent and the Grenadines (2022). None of these economies were under a Fund program arrangement at the time of the Article IV consultation.

the staff report. Overall, however, the Article IV documents reviewed indicate that the DSA frameworks direct the attention of desk economists to vulnerabilities stemming from debt structure and contingent liabilities.

42. **In terms of policy recommendations, in five of eight countries flagged by the DSA as at high risk of sovereign stress or debt distress, the staff report included substantive discussion and advice on debt management.** In two of these five cases, it also provided an annex on specific aspects of debt management. Some reference to debt management policies was included in an additional two of the eight staff reports on countries at high risk of sovereign stress or debt distress, but these discussions were not always fully developed. A fair conclusion is that issues related to debt management tend to be addressed in Article IV consultations of EMMIEs with elevated debt vulnerabilities, although there is some variability about the depth of the advice.

43. **Overall, however, Article IV reports tended to focus more heavily on "above-the-line" assumptions—e.g., sustainability of a given deficit under different scenarios—and less on "below-the-line" aspects.** Assumptions on how the deficit and maturing debt would be financed were typically not discussed in staff reports. Fund staff interviewed for this evaluation noted that country desks tend to pay more attention to above the line assumptions, partly due to their training as macroeconomists, and suggested that developing greater expertise and focus on financing aspects would be beneficial. Data availability was also mentioned by Fund staff as constraining their ability to comprehensively report or analyze these issues.

B. Other Aspects of Debt Management Advice in Article IV Staff Reports

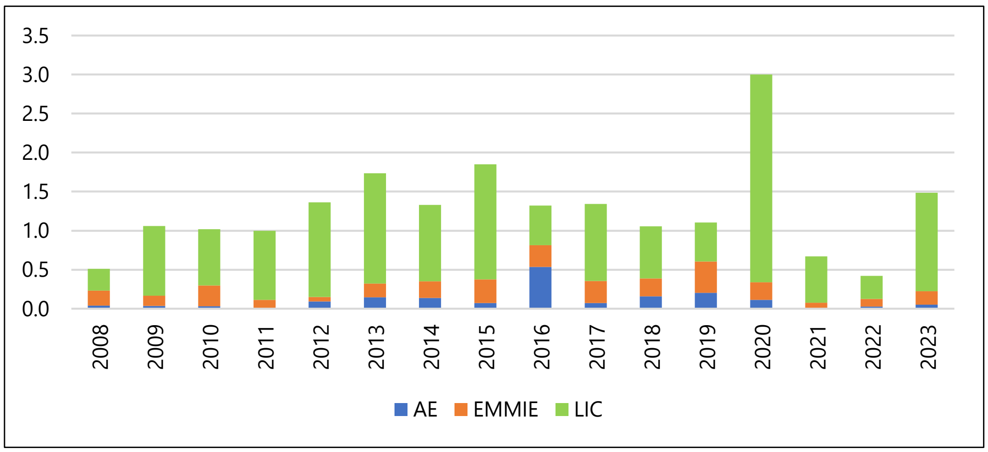
44. **An area of debt management that receives little discussion in Article IV reports is the operation of Debt Management Offices and related institutions and agencies of public debt management.** This is despite the considerable emphasis placed on these arrangements by the IMF and World Bank Guidelines. This parallels scant mention of the Guidelines and associated institutional aspects in the Fund's flagship reports. In terms of institutional arrangements, one academic study (Sadeh and Rubinson, 2017) has asked whether involvement with the IMF has encouraged members to create autonomous Debt Management Offices. The authors assemble a country-year database of national debt management legislation for 75 countries spanning the period 1950–2013. They capture IMF involvement by a variable measuring debt owed to the Fund (scaled by GDP or government consumption). They find little evidence that IMF involvement in a country encourages establishment of an autonomous Debt Management Office. However, there is some evidence of increased centralization of debt management functions in the finance ministry.[25]

[25] The IMF provides TA regarding institutional arrangements such as self-standing Debt Management Offices. The extent of such TA might be an alternative measure of IMF involvement. However, this could potentially introduce an endogeneity issue, given that TA is demand-driven and often reflects a country's existing intent to establish a DMO. It would also be interesting to extend the empirical analysis to a more recent period to assess whether the results of Sadeh and Rubinson (2017) still hold.

45. **A relevant question is whether Article IV reports draw timely attention to new issues and changing circumstances posing challenges for public debt management.** We focused specifically on the following two aspects:

- ***The emergence of new classes of creditors who may not yet participate in international public debt forums and for whom information on lending may be incomplete.*** As an example, we searched Article IV reports for the period 2008–23 and picked up 1,158 paragraphs referring to borrowing from China.[26] Figure 5 shows growing attention to borrowing from China in 2013 and 2015 and then two other spikes in 2020 and 2023, most heavily in Article IV reports on LICs.[27]

Figure 5. Coverage of Bilateral Borrowing from China in Article IV Reports
(Proportionate to total number of paragraphs in Article IV reports for country group)



Source: IEO staff calculations using FDET data.

- ***The attention paid to the relatively new issue of climate-related risks for the management of debt.*** Here the MAC SRDSF explicitly mandates the analysis of climate-related risks to the public finances, where appropriate. The LIC-DSF does not make the same provision although it does mandate the analysis of natural disasters in tailored stress tests (where the incidence of disasters may in some cases be climate related) for a small

[26] Bilateral lending from China has received significant attention by analysts, think tanks, and academics in recent years (e.g., Horn, Reinhart, and Trebesch, 2021; Gelpern and others, 2022; Moses, Springer and Gallagher, 2023). A rich database on Chinese lending activities is the China's Overseas Development Financed Database, managed by the Boston University Global Development Policy Center https://www.bu.edu/gdp/chinas-overseas-development-finance. While China is not a Paris Club lender, it has participated in the G-20 Common Framework for Debt Treatment (e.g., in the case of Zambia).

[27] Spot checks by IEO staff and consultants suggest that these are in fact references to lending by China to the countries in question—though it is important to bear in mind the limitations of tabulations of keywords in texts. Note that Figure 5 depicts mentions by year of publication of the Article IV report, not the year of consultation where these differ.

subset of countries. Moreover, the recently issued Supplement to the 2018 Guidance Note on the Debt Sustainability Framework for LICs (LIC-DSF) provides additional guidance and examples on how to account for risks stemming from climate change (IMF and World Bank, 2024). The IMF has already started work on the implications of climate finance for debt management (e.g., IMF 2022c; Ando and others, 2022; Chamon and others, 2022; Lindner and Chung, 2023).[28] Further discussion on how the Fund analyzes the impact of climate issues on debt sustainability and risks is deferred to the ongoing IEO evaluation on the IMF and climate.

VI. CAPACITY DEVELOPMENT ON PUBLIC DEBT MANAGEMENT

46. **CD activities are a critical channel for the Fund's bilateral engagement on public debt management.** As part of these activities, the IMF provides in-country TA and training, using staff based at Headquarters as well as regional debt managers and advisors stationed across seven regional technical assistance centers (IMF, 2024b; c). As an example of the intensity of the activity in this area, in recent years MCM (often jointly with other IMF departments and/or the World Bank) provided bilateral TA on debt management to 119 economies, including 60 EMMIEs. Often countries received multiple missions over a given period.[29]

47. **CD on debt management is financed by the Debt Management Facility (DMF), a multi-donor trust fund, as well as bilateral donors.** First introduced in 2008 by the World Bank, the DMF has been co-managed with Fund since 2014. Its primary mission is to strengthen debt management and sustainability analysis practices to mitigate debt-related risks and enhance transparency. This is achieved through TA, analytical studies, and training sessions. The DMF also fosters collaboration among TA providers and promotes dialogue on debt issues. As of June 30, 2024, 88 countries were eligible for the DMF, 31 of which were EMMIEs.[30] The DMF's Steering Committee is jointly chaired by the IMF and the World Bank. The committee offers strategic direction for the DMF establishing policies, approving the annual operational strategy, and evaluating performance.

48. **Available evidence points to a positive assessment of the effectiveness and usefulness of Fund's CD activities in the area of debt management.** In the context of a 2017 assessment of CD in country development of the MTDS, questionnaire responses from national officials indicated

[28] IMF (2022c) discusses challenges and opportunities for climate finance in LICs and EMMIEs as well as new instruments that have been developed to mobilize resources to finance adaptation and mitigation investments. Chamon and others (2022) discuss debt for climate swaps. Ando and others (2022) analyze green and catastrophe bond markets. Lindner and Chung (2023) provide guidance to issuers of sovereign ESG bonds, with a focus on Emerging Market and Developing Economies.

[29] A notable example of TA is the effort led by ICD to strengthen public debt projections and analysis of member countries, including through the recent creation of the Public Debt Dynamics Tool (Acosta-Ormaechea and Martinez, 2021; Cohen-Setton, Montiel, and Zoli, 2025).

[30] The latest list of eligible countries is available at https://www.dmfacility.org/sites/default/files/FY_2025.pdf .

that TA helped them to introduce a structured and coherent approach to designing a debt management strategy (IMF, 2017a).[31] Countries also appreciated advice on institutional and governance reforms and integrating debt management into macroeconomic policy formulation and implementation. Quantitative evidence on the effectiveness of Fund's TA on MTDS development is limited, in that it is available for a nonrandom sample of countries requesting Debt Management Performance Assessment (DeMPA) interventions and receiving Country Policy and Institutional Assessment (CPIA scores) as IDA eligible countries (IMF, 2017).[32] Other—though indirect—evidence on the effectiveness of Fund's CD on debt management is provided by two independent external evaluations of DMF performance, undertaken in 2013 and 2018, which found that the DMF has been relevant to the debt management capacity-building needs of DMF-eligible countries and effective in supporting capacity building (Universalia, 2013; 2018).[33]

49. **The review of Fund's TA reports on debt management suggests a shift over time from a focus on liability management to greater attention to institutional aspects.** For example, a 2008 TA report on public debt management in the Philippines (IMF, 2008) focused principally on the currency composition of government debt and exposure of the public-sector balance sheet to exchange-rate risk, supplemented by brief mentions of coordination of debt management with monetary policy, domestic debt market development, and risks associated with banking sector holdings of government debt. More recent reports, such as El Salvador (IMF, 2020c), Sri Lanka (IMF, 2020d) and Oman (IMF, 2021c). focus more heavily on institutional aspects (in Sri Lanka, fragmentation of debt management responsibilities and desirability of creating an autonomous Public Debt Management Administration or Office; in El Salvador, strengthening the National Directorate for Investment and Public Credit responsible for monitoring and controlling public borrowing, upgrading debt recording and reporting, and improving investor relations; in Oman, how the Debt Management Office might formulate, publish and implement a medium-term debt management strategy).[34]

[31] Though a response rate of some 50 percent signals the possibility of selectivity in the responses.

[32] DePMA is a methodology for assessing debt management practice by applying a comprehensive set of performance indicators (World Bank, 2015). Country Policy and Institutional Assessment scores are applied annually by the World Bank to IDA-eligible countries; these rate countries on a scale of 1 to 6 for four areas: economic management, structural policies, social inclusion and public-sector management and institutions (World Bank (nd)).

[33] The 2018 evaluation found that DMF-supported activities were highly relevant and valued for their expertise. The DMF excelled in developing and disseminating debt management capacity-building tools, aiding countries in adopting new methodologies and creating institutional structures. Significant progress was noted in countries preparing and approving MTDSs and conducting debt sustainability analyses. The DMF was less effective in areas like implementing debt management reforms, developing debt markets, accessing international capital markets, and conducting portfolio risk assessments. Recommendations included better coordination between upstream and downstream support, introducing client readiness assessments, and enhancing collaboration between debt management and public financial management providers at the country level.

[34] The diagnostic for El Salvador also devotes some attention to how the mix of external and domestic market financing might be adjusted to achieve the government's objective of reducing interest costs and reducing risks.

VII. COUNTRY CASES

50. **For a deeper analysis of Fund's bilateral advice on debt management, this section reviews three country cases, Jamaica, Sri Lanka, and Ecuador.** The Jamaica case is chosen to ascertain interactions between TA and surveillance in the area of debt management. Sri Lanka and Ecuador recently experienced a sovereign default and stress in the sovereign market, respectively, and their cases are chosen to assess whether the Fund preemptively warned the authorities about risks associated with their public debt and provided timely advice on managing these risks.

A. Jamaica

51. **Jamaica offers a case study of IMF advice on public debt management delivered through TA and Article IV surveillance.** Faced with an incipient debt crisis, in 2010 the Government of Jamaica completed a debt exchange, put in place a Fiscal Responsibility Framework, and entered a Stand-By Arrangement with the Fund. There was then a second debt exchange in 2013 and a revised Fiscal Responsibility Framework in March 2014 to include a fiscal rule limiting the debt/GDP ratio to no more than 60 percent by 2025/6 (a rule that was later amended to account for the impact of the Covid-19 pandemic).

52. **The Government was supported by TA missions from the IMF, World Bank and Inter-American Development Bank (IDB).** A TA mission from FAD visited Kingston in February/March 2010. It reviewed the Government's fiscal responsibility legislation, recommending clarification of key terms, principles and targets. It was critical of including a date for achieving fiscal targets so far in the future as to exceed the term of the current government. A second mission, mounted jointly by the IMF, World Bank and IDB next visited in May 2010 to assess the institutional and technical capacity of the Government's Debt Management Unit and lay the foundation for a medium-term debt management strategy. This mission focused on the debt exchange and its implications for interest-rate risk. It noted that Jamaica had issued an annual debt management strategy since 2000 but that this would benefit from more comprehensive analysis and clearer definition of objectives. It criticized debt management for focusing on short-term cost reduction at the expense of developing a medium-term framework for fiscal and debt sustainability. It recommended investing in stronger in-house technical capacity and establishing a high-level Debt Management Committee to develop debt management strategies. It concluded with an action plan, distinguishing tasks for the short and medium terms, and designating one of the three participating multilaterals as the principal source of assistance for each aspect.

53. **While the IMF and collaborators provided extensive TA at a critical time, this did not consistently and comprehensively feed through into bilateral surveillance.** The staff report for the 2009 Article IV consultation (approved in January 2010) anticipated the need for a comprehensive MTDS but did not elaborate. The staff report for the 2011 Article IV (May 2012) treated debt management in one paragraph. It recommended early improvement of the new public debt law, steps to improve the debt profile and reduce the interest bill, strengthening the

Debt Management Unit, enhanced cash management by public sector agencies, increased use of auctions, and improved communication with investors. The staff report for the 2014 Article IV (June 2014) did not touch on public debt management.

54. **Jamaica's authorities interviewed for this evaluation expressed positive views of the quality and usefulness on Fund's TA on debt management.** They underscored that Fund TA continued to provide critical advice in 2014–16, helping in setting up an auction system, creating an agreement between the fiscal agency and the Bank of Jamaica to avoid duplication of efforts and costs. TA also helped to enhance the MTDS and mitigate portfolio risks. Overall, TA during that period was regarded as adequately tailored and key in supporting very significant reforms. The authorities also pointed out that consultation with MCM in the context of the Article IV were critical for identifying Jamaica's TA needs.

B. Sri Lanka

55. **This section examines the Fund's public management advice in the years leading up to Sri Lanka's 2022 sovereign default to assess whether the Fund issued early warnings about debt risks and offered timely guidance on addressing them.[35]** Fund engagement with Sri Lanka was intense between 2016 and 2019, as the country implemented an adjustment program, supported under the Extended Fund Facility (EFF), envisaging fiscal consolidation. The IMF, together with the World Bank also provided TA to support authorities' effort to formulate a MTDS, create an independent public debt management agency, and enhance the government security market (IMF and World Bank, 2017; IMF, 2020d).

56. **Program implementation was disrupted by a combination of major unforeseen shocks and domestic policy choices.** They included a drought in 2017, political turmoil in 2018, and a severe domestic terrorist attack in 2019, as well as the reversal in fiscal adjustment in late 2019, against Fund's advice. As the Covid-19 pandemic erupted, Sri Lanka's EMBI spread rose sharply and its sovereign credit ratings were downgraded. Access to international capital markets was lost in the spring of 2020 and the large deficit was financed by the central bank. Public debt reached over 114 percent of GDP in 2021, also because of guarantees to cover SOE losses.

57. **The 2021 Article IV staff report was very explicit in warning about rollover risks going forward and recommended measures to mitigate them.** It advocated a comprehensive adjustment, and also indicated that "in staff view, fiscal consolidation and macroeconomic policy adjustments alone could not restore Sri Lanka's debt sustainability," implicitly hinting to the potential need for debt reprofiling (IMF, 2021d). The authorities acknowledged the magnitude of the challenges but viewed the outlook presented by staff as overly pessimistic and believed that ongoing challenges could be addressed by a roadmap they had announced. The eruption of the war in Ukraine in early 2022 deepened Sri Lanka's challenges further, and the country formally defaulted on their international sovereign bonds in May 2022.

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[35] More background on this case is presented in the Annex.

58. **Sri Lanka's authorities interviewed for this evaluation indicated that Fund's advice during the 2016–19 program was sound, but that public support for the program was lacking.** The tax cuts introduced by the new administration, which resulted in widening deficits, as well as subsequent policy choices were key factors contributing to the sovereign default. The authorities indicated that a bunching of maturities in 2018 created problems for debt management but did not confirm that the Fund helped them anticipate these challenges (that bunching of maturities was not mentioned in the 2018 Article IV report). In 2020, the DSA indicated that Sri Lanka's debt had become unsustainable, but the authorities did not agree with Fund's assessment. After the 2022 default, the government undertook a restructuring and negotiated a new program with the Fund. The authorities also indicated that Fund's TA had provided advice on the institutional set up for the debt management function. (We would note that the desirability of these institutional reforms was highlighted in the 2018 Article IV report.) A Public Debt Management Act was approved by Parliament in 2024, and a Public Debt Management Office is expected to become operative next year.

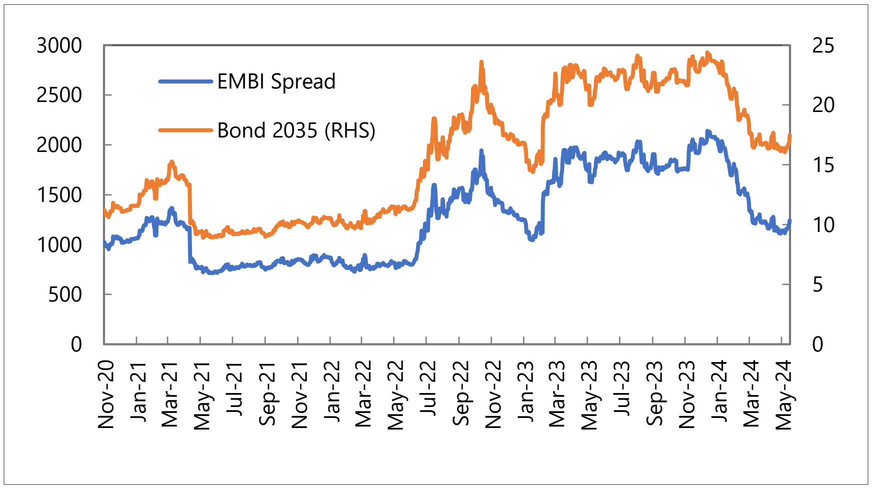
C. Ecuador

59. **As Ecuador experienced significant sovereign stress in 2022–23, after a successful conclusion of a Fund program, this case is analyzed to evaluate whether the Fund timely highlighted debt risks and provided advice to help address them.[36]** The country had implemented a Fund supported program in 2020–22, which helped to mitigate the impact of the Covid-19 pandemic, put public finances on a more sustainable path and strengthen domestic institutions and policy frameworks (including through a landmark reform in fiscal governance, which also introduced a new debt limit). Fund TA supported the launch of a MTDS in February 2021, the publication of more transparent and timely debt statistics, and introduction of a new fiscal rule.[37] The program was regarded as good example of successfully integrating capacity development and program design in the ex post evaluation (IMF, 2023d). Despite these achievements, Ecuador's sovereign yields and spreads increased sharply in the summer of 2022, reflecting investor concerns about protracted domestic protests, worsening of the domestic security situation, and tighter financing conditions for EMMIEs (Figure 6). Higher borrowing costs forced the authorities to postpone market access.

[36] In 2020 Ecuador completed a debt restructuring operation necessary for debt sustainability before the Fund could proceed with an arrangement. During the restructuring process, the Fund provided guidance and technical support, helped the stakeholders understand the complexities of the debt structure, and explained the benefits of the operation while staying outside of the negotiations. Overall, the 2020 debt restructuring was seen as a success (Alfaro and de Las Casas, 2024).

[37] The IMF has provided intensive TA support on debt management to Ecuador over 2018–2020. An IMF mission gave training on the MTDS and Annual Borrowing Plan in September 2022.

Figure 6. Ecuador: EMBI Spread and Bond Yield
(In daily basis points and percent)



Source: IMF (2024d).

60. **At the time of the final review of the Fund program in December 2022, the SRDSF assessment was fairly benign.** It assessed the overall risk of sovereign stress as low, due to "a moderate level of vulnerability in the medium-term mitigated by the credibility of the ongoing fiscal consolidation underpinned by the IMF program."[38] The SRDSF pointed out risks to downside risks in the event of fiscal policy slippages, faltering recovery, and lower oil prices, but also highlighted low debt service and long maturities as mitigating factors.

61. **Yet, sovereign spreads and yields soared in 2023, amid an unanticipated political crisis and unforeseen shocks.** Sudden political turmoil and unexpected general and presidential elections prevented further progress with the fiscal and institutional reform plan (IMF, 2024d). Ecuador's fiscal position deteriorated due to a sharp drop in oil revenues, a substantial rise in external debt interest payments driven by global monetary tightening, and policy slippages. Fund engagement with Ecuador was limited in 2023, as the country was undergoing l elections. With the country out of international capital markets, also because of the worsening domestic security crisis, treasury deposits and foreign exchange reserves plunged. Ecuador requested a 48-month Fund arrangement in 2024. Unexpected political and external shocks, policy slippages, and the domestic security crisis all contributed to Ecuador's sovereign stress; yet, the disconnect between a fairly benign SRDSF and the large increase in gross financing needs that led to a significant decline in government liquidity buffers is somewhat puzzling.[39] It indicates that perhaps debt

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[38] In September 2022, the government of Ecuador had reached an agreement with the Chinese Development Bank and China Exim Bank to reprofile 78 percent of the country's debt to China.

[39] The SRDSF was still in a pilot phase at that stage, with several modules not yet operational.

risks, including from policy reversals and interest rate shocks, were not fully reflected in the Fund assessment at the end of 2022.[40]

62. **Ecuadorian officials interviewed for this evaluation stated that the advice received from the Fund on fiscal risk monitoring and debt management was useful, timely, and practicable.** The Fund provided helpful recommendations on extending debt maturities and enhancing the quality and transparency of debt data. Officials recognized that the Fund's assessment of risk of sovereign stress in 2022 could not anticipate some of the subsequent shocks (e.g., oil production disruptions, political crisis). Nevertheless, the Fund underestimated the risks of policy reversal and political risks, considering Ecuador's high political fragmentation and long history of difficult political transitions. Officials argued that the absence of exchange rate volatility and devaluation risks owing to Ecuador's dollarization might have contributed to the perception of lower sovereign distress risk in Fund's assessment. In that regard they pointed out that deeper analysis and more tailored adaptation of Fund's advice to dollarized economies would be useful.

VIII. ASSESSMENT

Overall

63. **The Fund is providing valuable support to countries with debt management challenges, through dedicated initiatives, capacity development, and regular surveillance** Coordination of TA on debt management, both within the Fund and between the Fund and the Bank, is relatively smooth. These positive results reflect a common understanding across the Fund of the importance of both debt sustainability and sound risk management, the provision of significant staff resources, a reasonably clear delineation of responsibilities, and explicit frameworks for cooperation both within the Fund and between the Fund and other stakeholders.

64. **The IMF together with the World Bank has periodically invested in the development of comprehensive and valuable "Guidelines" for debt management, which adopt both quantitative and institutional perspectives.** Again, in collaboration with the World Bank, the Fund has developed a framework to help country authorities design a medium-term debt management strategy. It has launched initiatives to strengthen public debt transparency through capacity building in the area of debt recording and data reporting. It has developed a Fiscal Transparency Code and conducted Fiscal Transparency Evaluations.

65. **The Fund has provided relevant advice on vulnerabilities from debt profile and debt management through multilateral and bilateral surveillance.** The Fund has periodically revised the tools to assess debt sustainability, with the MAC framework having an increased focus on identifying liquidity risks and vulnerabilities stemming from debt composition and

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[40] According to a recent IEO evaluation, authorities and experts interviewed with reference to Ecuador's 2020–22 Fund program, expressed the view that markets "were always wary of Ecuador's political volatility and institutional weakness," despite recognizing the authorities' goodwill (Alfaro and de Las Casas, 2024b).

contingent liabilities. Our review of a sample of Article IV reports for 12 EMMIEs indicates that desk economists have paid attention to vulnerabilities arising from debt structure and contingent liabilities, and have often provided specific policy recommendations on debt management for countries with elevated debt. In addition, Article IV reports paid attention to emerging issues and changing circumstances in the area of public debt management, such as increasing bilateral borrowing from China and climate finance.

66. **The Fund has mounted useful bilateral TA missions addressing aspects of debt management at the request of the government of the country concerned.** These activities have been frequent, have covered a wide range of topics and member countries. Based on available evidence, including interviews with country officials conducted for this evaluation, TA in this area is valued by national authorities and considered helpful in fostering their ability to manage public debt.

67. **That said, there is room for further improvements.** These include: (i) enhanced coordination across surveillance activities and TA; (ii) maintain close coordination across departments and with the World Bank; (iii) updating of DSA frameworks; and (iv) enhancing data on debt and on institutional aspects of debt management, especially in light of the emergence of new creditor classes and new instruments.

(i) Enhanced Coordination Across Multilateral and Bilateral Policy Advice

68. **Systematic integration of institutional and TA advice in bilateral surveillance would enhance the effectiveness of the Fund's advice on public debt management.** The Fund's initiatives in the area of debt management, though, are not always well coordinated with one another or with the Fund's other activities. The "Guidelines" and other analysis conducted by the IMF's functional departments are not much mentioned in the Fund's flagship reports. Institutional aspects of debt management emphasized in the Guidelines that are the subject of TA are mentioned only briefly, if they are mentioned at all, in Article IV reports. IMF staff report the existence of interaction between TA and Article IV reviews: sometimes issues flagged during TA are followed up in Article IV reviews. Other times issues turned up during Article IV reviews lead to requests for TA. To better integrate TA and surveillance, there may be a case for institutionalizing a systematic feedback loop from debt vulnerability assessments to TA on debt management. While TA is demand driven, if surveillance (through Article IV consultations or other methods, such as the IMF-FSB Early Warning Exercise) detects specific vulnerabilities early enough, area departments could suggest TA to the authorities while alerting the functional departments to direct resources accordingly. The importance of further strengthening the integration of CD with the Fund's surveillance more generally was recently reaffirmed by the 2024 review of the CD strategy, even as it recognized the significant advances made since the 2018 Strategy Review (IMF, 2024e).

69. **More attention to below-the-line aspects of deficit finance in warranted**. Article IV reports have a heavy focus on "above-the-line assumptions" (how large a deficit is sustainable); less attention to devoted to below-the-line aspects (how that deficit—and inherited debt—

should be financed). A more holistic view would place more emphasis on this "financeability" aspect. This is obviously the case in the context of a program, where the IMF's mandate requires it to confirm that programs are fully financed.[41] To do this credibly in the context of surveillance, the Fund would need additional resources to fully analyze the risk of sovereign debt portfolios.

(ii) Maintaining Close Coordination Across Departments and the World Bank

70. **Coordination across departments seems generally good, with a clear division of labor.** Reviews of Article IV reports by functional departments focus on different aspects of debt management. Thus, whereas FAD is more concerned with the "above the line" portion of the fiscal accounts (budget planning and execution, medium-term fiscal framework, fiscal transparency), MCMDM focuses on the "below the line" aspects (how the resulting debt is financed and managed, market development etc.), although FAD also supports capacity development in cash management and government cash flow forecasting. Country teams in area departments play a central role in shaping debt-related advice by gathering information from the authorities, developing the macroeconomic framework, and integrating inputs from functional departments. Debt sustainability analysis comes under the purview of SPR, although it is often prepared by country teams. Where institutional changes have legislative or statutory prerequisites, there may also be interaction with the Legal Department. The review process fosters dialog between functional and area departments.

71. **These different departments naturally focus on different aspects of debt management, so close coordination is essential.** Some departmental analyses emphasize the minimization of debt service costs, through inter alia choice of currency-denomination and maturity structure of the debt, and by improving investor relations. Others emphasize steps to limit crisis risk. Still others highlight the need for institutional initiatives, to inter alia improve the transparency, comprehensiveness and accuracy of debt statistics. These different emphases are not always aligned with one another. Ensuring close coordination across departments as well as within the different divisions within departments is therefore crucial to maximize the quality, timeliness, and comprehensiveness of Fund advice to members. In this respect, departments should regularly assess and review their coordination procedures to identify areas for improvement and in order to keep procedures agile and responsive to changing circumstances and priorities.

72. **Coordination with the World Bank seems close, perhaps closer than in any other issue area.** The two institutions coordinated in producing two iterations of the "Guidelines," as noted above. They regularly coordinate the provision of TA on debt-related issues such as local market development. Much of this work is supported by the Debt Management Facility, a multi-donor trust fund jointly managed by the Fund and Bank since 2014. Its management involves a monthly coordination meeting at which information about specific countries is discussed. The

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[41] The August 15, 2024 Supplement Guidance Note on LICs, which puts more emphasis on the assessment of overall debt vulnerabilities, is an improvement. [Supplement to 2018 Guidance Note on the Bank-Fund Debt Sustainability Framework for Low Income Countries (imf.org)](#) (note that it lies outside the review period).

existence of this facility thus ensures that IMF and World Bank staff concerned with debt management remain in regular contact. This collaboration limits the risk of conflicting recommendations between the two institutions. Moreover, the institutions collaborate on other key initiatives, such as the MPA, the MTDS framework and the local currency bond market framework. The ongoing evaluation on debt issues in LICs will evaluate the coordination between the Fund and the World Bank more closely.

(iii) Updating of DSA Frameworks

73. **The debt sustainability frameworks for MACs and LICs may have been revised repeatedly, but they nonetheless warrant revisiting.** The framework for MACs utilizes a logit model to classify countries as at High or Medium/Low risk of debt distress. The stability over time of this model is not clear. Crisis-prediction models have a checkered history. At a minimum, such models should be regularly re-estimated as additional data become available. Similarly, the thresholds for prudent debt levels used in the analysis of LICs appear arbitrary. Whether they are unchanged over time should be analyzed, not assumed. The thresholds specified could be better justified. The ongoing comprehensive review of the LIC-DSF provides a not-to-be-missed opportunity to address limitations of the current framework.

74. **It is crucial for the Fund to be ahead of the curve on raising issues and new challenges for debt management, including the development of new debt instruments.** It is encouraging that the IMF has already started work on the implications of climate finance for debt management. The Fund's activities in this area will be explored further in the ongoing evaluation on the IMF and Climate Change. The Fund also needs to stay abreast with evolving country practices in public debt management and reflect them in its advice. In this respect, the Fund could consider whether a further revision of the 2014 debt management guidelines is warranted within the next few years. An aspect on which the Fund could intensify its advice on the Sovereign Asset and Liability Management (SALM) approach, which can have significant advantages over separate management of assets and liabilities, and on which the Fund has already done analytical work. Other challenges and opportunities for public debt management are posed by the rise in digital finance, Fintech and artificial intelligence.

(iv) Enhanced Data on Debt and Debt Management

75. **Although the IMF maintains several databases, often in collaboration with other IFIs, these do not fully provide the desired coverage and disaggregation.** The Global Debt Database and the Quarterly Public Sector Debt comprehensive in particular seem to include a fairly detailed data breakdown. Nevertheless, the accuracy and completeness of the data reported to and disseminated through these platforms warrant close examination. For instance, the involvement of nontraditional creditors—such as official lenders outside the Paris Club—and the emergence of new types of liabilities, including loan contracts with extensive confidentiality clauses that prevent borrowers from disclosing their terms or even their existence, raise concerns about the adequacy of current statistics on bilateral official debt stocks and flows.

76. **A one-stop shop for data on public debt by currency, maturity, creditor etc. is missing.** Some of this information is available for the subset of IMF members subscribing to the General Data Dissemination and Special Data Dissemination Standards, but participation is voluntary. Moreover, differences in coverage and reporting methodologies among the various databases may lead to inconsistencies. There may be a reluctance to invest in construction and maintenance of this kind of comprehensive dataset on the grounds that important data gaps (on, inter alia, bilateral official lending) would undermine reliability. To be sure, the costs of expanding and updating such a database would be considerable. But the benefits would also be significant. Against this background, the 2024 Review of Data Provision to the Fund has proposed a substantial update to the overall envelope of data requirements in the areas of public sector (IMF, 2024f). The cooperation and commitment of all IMF member countries to improving the transparency of their debt statistics is critical for enhancing the quality of current and future databases.[42]

77. **One approach to addressing this issue would be even closer coordination with the World Bank on debt data.** For instance, the Bank maintains an additional database, International Debt Statistics, which provides itemized data on external debt, distinguishing long-term and short-term debt, and debt owed to official creditors, bilateral creditors and multilateral creditors and private creditors (where the last category distinguishes bonds and debt owed to banks). The Bank is presumably more concerned with the ability of governments to finance projects and general development needs, whereas the Fund is more concerned with crisis risk. Further collaboration between the two institutions would facilitate the development of a database suited to both aspects. On domestic public debt, which is often underreported compared to external debt, the Fund is working with the World Bank to expand the scope of the World Bank's Debt Reporting System to include public domestic debt on a voluntary basis, which would represent a significant step towards transparency.[43]

78. **The Fund could usefully develop a database with information on Debt Management Offices in member countries.** As noted earlier, debt management issues can be approached from two perspectives: numerical statistics on debt aggregates, and institutional aspects of debt management issues. While FAD maintains databases on other debt- and deficit-related institutions (i.e., presence or absence of independent fiscal councils), the Fund does not maintain a database on the presence or absence of Debt Management Offices and whether a government consolidates responsibility for debt management in a single ministry. Systematic data on this aspect would be a useful resource for desk economists and encourage peer-to-peer learning on the part of members. Building such a database would require additional resources.

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[42] See IMF (2023a) for a discussion of legal and operational challenges to the disclosure and reconciliation of high granularity public debt.

[43] Currently, the Debt Reporting System mandates only the reporting of detailed external debt data for countries receiving International Bank or Development Assistance loans.

ANNEX I. FUND'S ADVICE ON PUBLIC MANAGEMENT IN THE YEARS PRECEDING A SOVEREIGN DEFAULT—THE CASE OF SRI LANKA

Sri Lanka defaulted on its external government debt in 2022, triggering social unrest and political instability This section reviews Fund's engagement with the country and advice on public management in the years preceding the sovereign default.

Fund engagement with Sri Lanka was intense between 2016 and 2019. In 2016 the country embarked on an adjustment program, supported under the Extended Fund Facility (EFF), to address macroeconomic imbalances and vulnerabilities, including a central government debt at 75 percent of GDP.[1] The IMF program envisaged fiscal consolidation and reform measures, including revenue mobilization, public financial management reform, and state enterprise reforms. Initially, important progress was achieved through fiscal adjustment, other prudent macroeconomic policies, and key reforms, such as a new income tax law and automatic fuel prices adjustments to support profitability in the state-owned enterprises (SOE) sector.

At the same time, the IMF, together with the World Bank, provided technical assistance (TA). It supported authorities' effort to formulate a MTDS, create an independent public debt management agency, and enhance the government security market (IMF, 2020b; IMF and WB, 2017).[2] The strategy to manage sovereign bond maturities for 2019–22 was approved by cabinet in January 2018; a Liability Management Act was enacted in March 2018; the MTDS for 2019–23 was launched in April 2019; and a plan to establish a public debt management agency was approved by the cabinet in October 2019. The Fund also provided TA to improve public sector debt statistics (IMF, 2019c). Advice from TA was also reflected in staff reports for program reviews.

However, program implementation was challenged by large unexpected shocks, including a drought in 2017, political turmoil in 2018, and a severe domestic terrorist attack in 2019. Public debt, including publicly guaranteed debt and Fund credit outstanding, increased to 91 percent of GDP at end-2018, reflecting weaker economic performance and the sizable currency depreciation. Moreover, following the Presidential and Parliamentary elections in late 2019, fiscal adjustment was reversed. The income tax and VAT were reduced; mechanisms in place to mitigate fiscal risks from SOEs were discontinued and plans to upgrade legislation relating to the fiscal rules were suspended. The IMF program stalled, and the arrangement expired in June 2020. Sri Lanka entered the COVID-19 pandemic with high debt level and low reserves. The 2019 tax cuts as well as the impact of the pandemic on revenues and spending

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[1] According to the debt sustainability analysis included in the Staff Report for the 2016 Article IV Consultation and Request for a Three-Year Extended Arrangement under the Extended Fund Facility, the debt profile indicated moderate degree of vulnerabilities related to external financing requirements, debt held by non-residents, and debt denominated in foreign currency (IMF, 2016c).

[2] The TA Report on the Institutional Framework for Public Debt Management (IMF, 2020b) highlighted that the debt portfolio was vulnerable to currency and interest rate shocks, and subject to rollover risks.

widened fiscal deficits to 12.2 percent of GDP in 2020. Sri Lanka's EMBI spread rose sharply that year, peaking at over 2,400 basis points and its sovereign credit ratings were downgraded several times, to CCC in the fall of 2020. Access to international capital markets was lost in the spring of 2020.

Table AI.1. Sri Lanka: Macroeconomic Indicators, 2015–22

	2015	2016	2017	2018	2019	2020	2021	2022
Growth and inflation (in percent)								
Real GDP growth	4.2	5.1	6.5	2.3	-0.2	-4.6	3.5	-7.8
Inflation (end-of-period, in percent)	4.6	4.4	7.1	2.8	4.8	4.2	12.1	54.5
Fiscal Indicators (in percent of GDP)								
Central governemnt balance	-6.6	-5.0	-5.1	-5.0	-7.5	-12.2	-11.7	-10.2
Central government gross financing needs	20.7	17.4	18.3	19.6	21.7	26.1	31.0	34.1
Central governemnt debt	76.3	75.0	72.3	83.6	82.6	96.7	102.7	115.5
Public debt[1]	82.1	84.1	82.7	91.0	89.0	104.0	114.3	126.3
Share of central debt in foreign currency (percent)	46.9	46.7	48.5	56.2	52.6	47.6	43.1	52.7

Sources: WEO; various IMF Country Reports.
1 Comparing central government debt, publicly guaranteed debt, Fund credit outstanding and international currency swap arrangements.

Large fiscal deficits persisted in 2021, at 11.7 percent of GDP. As a result, and because of new guarantees, largely to cover the losses of one SOE, public debt (including guaranteed debt and Fund credit outstanding) reached over 114 percent of GDP in 2021. The loss of access to international capital markets and foreign investors' exit from the local currency debt market created a large budget financing gap. This led to sizable central bank budget financing, contributing to a surge inflation. The 2021 Article IV staff report was very explicit in warning about high debt rollover risks going forward. It stressed that Sri Lanka's debt overhang and persistent fiscal and balance of payments financing shortfalls would constrain growth and jeopardize macroeconomic stability in both the near and medium term.

The authorities had presented a roadmap to tackle the crisis.[3] The 2021 Article IV staff report stressed that the authorities' plan was unlikely to address rollover risks and advocated a comprehensive set of fiscal, monetary, and exchange rate policies to restore macroeconomic stability. It also indicated, "in staff view, fiscal consolidation and macroeconomic policy adjustments alone could not restore Sri Lanka's debt sustainability"—implicitly hinting to the potential need for debt reprofiling. The authorities acknowledged the magnitude of the challenges but viewed the outlook presented by staff as overly pessimistic. They considered the

[3] The authorities announced a 6-month Roadmap in October 2021, envisaging to address near-term FX shortages by raising new financing from government-to-government loans and currency swaps with foreign central banks, expediting state asset sales, and tightening export surrender requirements.

debt and balance of payments challenges as a temporary problem, that could be addressed through the Roadmap they had announced.[4]

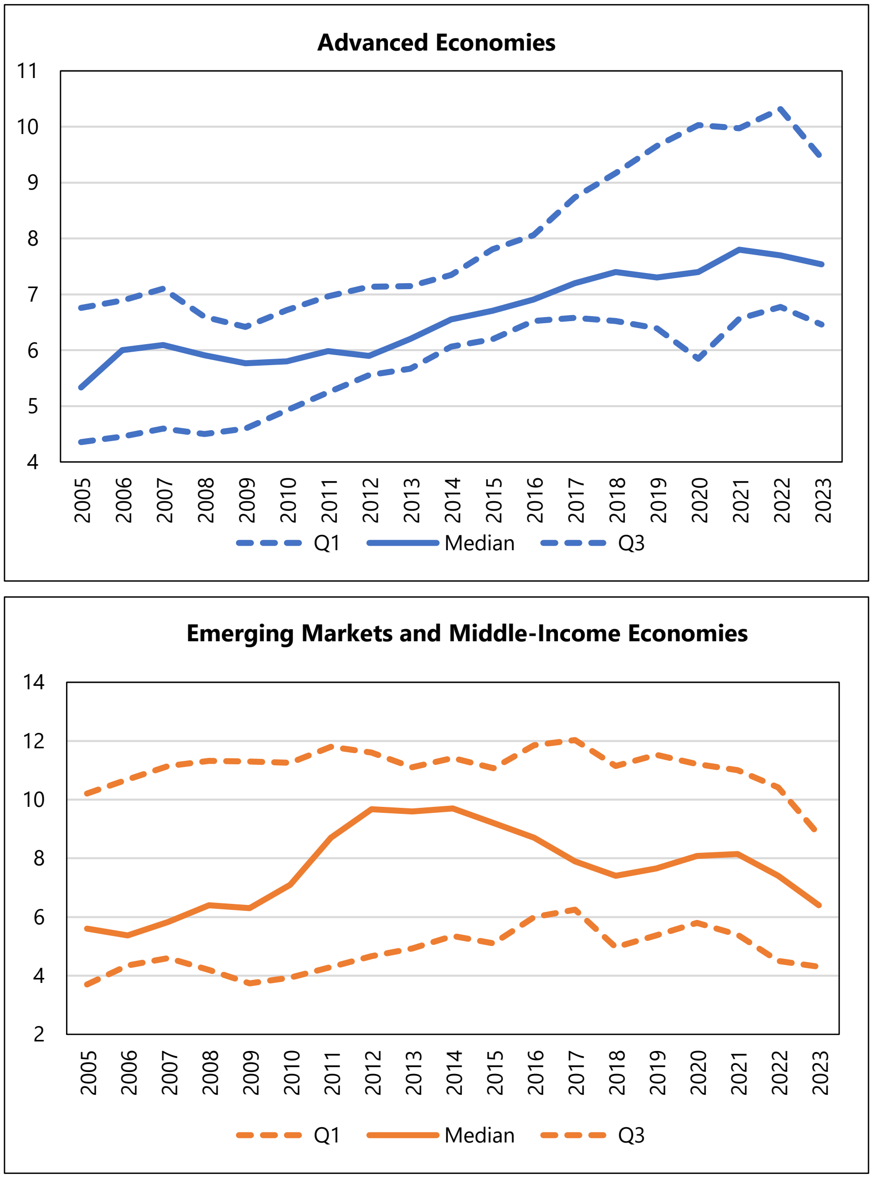
The eruption of the war in Ukraine in early 2022 deepened Sri Lanka's challenges further, given the heavy reliance on tourism and energy consumption. Reserves were soon depleted; the authorities suspended external debt service on April 12, 2022, and formally defaulted on their international sovereign bonds (ISBs) on May 18, 2022. Following the authorities' request in April 2022, IMF staff and the authorities reached a staff-level agreement on a 48-month arrangement under the Extended Fund Facility on September 1, 2022. The Sri Lanka's authorities started engaging in a dialogue with official and private creditors to achieve a durable solution to the debt crisis.

Overall, the Sri Lanka case indicates that the country's sovereign default was the result of a combination of a series of severe shocks as well as authorities' policy decisions. The Fund provided TA to support the institutional framework for public debt management and formulate a MTDS. Bilateral surveillance under Article IV highlighted significant rollover risks and stressed the need for a comprehensive adjustment program to restore macroeconomic stability, ahead of the 2022 default. However, because of external shocks and the country policy actions macroeconomic stability was jeopardized.

[4] See Authorities' Views section of the 2021 Article IV Staff Report.

APPENDIX I. ADDITIONAL DEBT INDICATORS

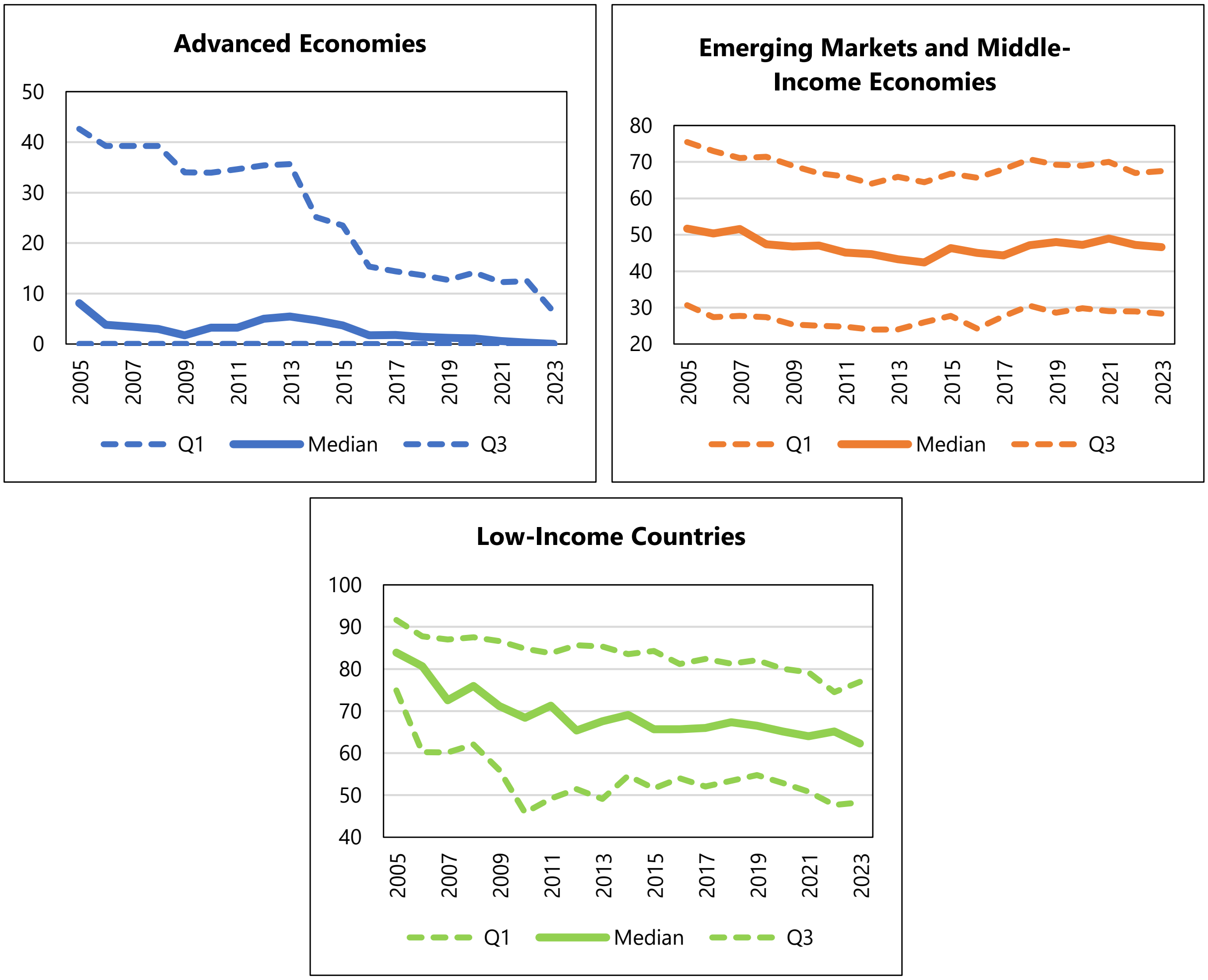
Figure AI.1. Maturity of Remaining Domestic Debt Securities
(Median, years)



Sources: BIS; IEO staff calculations.

Figure AI.2. Foreign-Currency Denominated Government Debt

(General government, percentage of total debt)



Sources: WEO; IEO staff calculations.

Appendix II. List of Keywords Used in Text Analysis in Figures 3 and 4

Public debt management, government debt management, sovereign debt management, public debt strategy, government debt strategy, sovereign debt strategy, public debt portfolio, government debt portfolio, sovereign debt portfolio, public debt portfolios, government debt portfolios, sovereign debt portfolios, government debt structure, public debt structure, sovereign debt structure, government debt structures, public debt structures, sovereign debt structures, contingent liabilities *and* government *or* public *or* sovereign, contingent liability *and* government *or* public *or* sovereign, public debt *and* maturity *or* maturities *or* currency *or* currencies *or* interest rate *or* interest rates, government debt *and* maturity *or* maturities *or* currency *or* currencies *or* interest rate *or* interest rates, sovereign debt *and* maturity *or* maturities *or* currency *or* currencies *or* interest rate *or* interest rates.

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CHAPTER 4—MILITARY SPENDING IN IMF FISCAL POLICY ADVICE

Prepared by Sanjeev Gupta*

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

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EXECUTIVE SUMMARY

This chapter examines the coverage of military spending by the IMF from 2008 to 2023 and highlights the need for the Fund to integrate military expenditure into its fiscal policy recommendations more systematically. Following the collapse of the Soviet Union in 1991, global military spending as a share of GDP nearly halved from its peak during the 1970–90 period, yielding a substantial peace dividend for all country groups. However, since 2014, especially after Russia's annexation of Crimea, military expenditures have increased significantly in many nations, especially in advanced economies, driven largely by geopolitical tensions.

Assessing the macroeconomic and spillover effects of military spending at the country level is challenging. Nonetheless, the rise in military expenditure raises concerns about the potential crowding out of critical investments in health, education, and infrastructure, as well as the risk of increased fiscal deficits and external debt, particularly in fragile and conflict-affected states. Despite the clear macroeconomic relevance, military spending received relatively limited attention in the Fund's flagship and country staff reports between 2008 and 2023.

When addressed, the Fund's treatment of military spending was consistent with its mandate and Executive Board decisions and guidance. Staff reports primarily focused on the fiscal and macroeconomic implications, such as balance of payments impacts or risks to domestic stability, without opining on national security priorities or the appropriate level of military expenditures—issues firmly within the sovereign domain of member governments. In its multilateral surveillance, the coverage was confined mainly to global or regional macroeconomic effects of military spending.

The Fund's coverage of military spending was uneven across countries. It is unclear why staff addressed military spending explicitly in some countries with above-average military expenditures in their budgets, alongside elevated fiscal deficits and debt-to-GDP ratios, while neglecting to do so in others. Such variation could be attributed to country-specific factors, including financing constraints and debt sustainability concerns. Moreover, a policy shift in March 2023—permitting Fund financial support for countries facing "exceptionally high uncertainty" due to external shocks—further complicates comparisons between recent scenarios, like that of Ukraine, with those prior to 2023.

To strengthen its fiscal policy advice, the Fund could adopt consistent terminology regarding military spending; address military expenditures in flagship publications in light of evolving geopolitical dynamics and the decision by several countries to raise military spending; ensure evenhanded treatment of countries facing similar macroeconomic conditions and levels of military spending; integrate off-budget military spending into debt sustainability assessments; and promote transparency in budgets, including military allocations.

I. INTRODUCTION

1. **Military spending has increased in several regions, reflecting changing geopolitical dynamics and escalating conflicts.** In AEs, the increase was particularly marked following Russia's invasion of Crimea in 2014. After the collapse of the Soviet Union in 1991, global military spending as a percentage of GDP nearly halved from its peak during the 1970–90 period, generating a significant peace dividend for all country groups

2. **The renewed rise in military expenditures has implications for the composition of government budgets and the economic growth prospects of countries, as it may crowd out more productive investments in growth-enhancing sectors.** While defense and the maintenance of law and order are essential for the smooth functioning of any economy, and military spending is often necessary to counter external threats, relatively high military budgets could raise important concerns. These concerns extend to the macroeconomic implications of policy choices exercised by individual countries, potentially necessitating attention within the framework of IMF surveillance of member policies and program support. The macro-criticality of military spending is thus highly context specific.

3. **The analysis of military spending primarily relies on data from the Stockholm International Peace Research Institute (SIPRI).[1]** Military spending encompasses expenditure on personnel (including pensions), weapons, operations and maintenance, research and development (R&D), military aid, and construction. Government Finance Statistics (GFS) also compiles data on military spending, although only for a limited number of countries. Additionally, GFS tracks expenditures related to law enforcement, including spending on police, prisons, and courts. When combined with military spending, this broader category can reflect a country's total spending on security. However, the Fund's mandate is on military spending as discussed in Section III. Thus, the focus of this chapter is on military spending narrowly defined.

4. **This chapter assesses three key issues during the evaluation of the period 2008–23: (i) the consistency of the Fund's engagement in military spending with its mandate and Executive Board decisions; (ii) the relevance of the Fund's advice on military spending in terms of its added value; and (iii) the evenhandedness of the advice, i.e., whether the Fund's treatment of military spending consistent across member countries given country-specific circumstances.** It is structured as follows: Section II examines recent trends in global military expenditures and the main macroeconomic implications and spillover effects of military

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[1] Several IMF flagship reports have used SIPRI data for cross-country analysis. See, for example, World Economic Outlook, October 1999; African Regional Economic Outlook, October 2021; and Middle Eastern Regional Economic Outlook, October 2018. SIPRI's Military Expenditure Database, which is updated annually, contains consistent time series on the military spending of countries for the period 1949–2023 and is based on official data provided by national governments. As noted in Section III, the authorities' submission of military spending data to IMF staff is voluntary. However, SIPRI regularly publishes such data with a one-year lag, which staff can use if the authorities do not provide the relevant information. Staff may bring deficiencies in military spending data to the attention of the Executive Board.

spending. Section III discusses the rationale for Fund involvement in military spending issues and the Fund's multilateral and bilateral policy advice on military spending between 2008 and 2023. Finally, Section IV concludes and suggests ways forward.

II. MILITARY SPENDING AND ITS MACROECONOMIC IMPLICATIONS

5. **Assessing the macroeconomic implications and spillovers of military spending in a given country is inherently complex.** For instance, in fragile and conflict-affected states (FCS), increased military expenditures may yield short-term benefits by enhancing security and stabilizing socio-economic conditions. However, over time, such spending can begin to crowd out more productive spending. Understanding the effects of military spending—whether domestic or cross-border—are positive, negative, or neutral depends on a range of factors. Identifying the tipping point at which the benefits wane requires access to reliable data and careful, context-specific analysis. This section addresses recent trends in military spending, its macroeconomic implications on growth and the fiscal accounts, and the tradeoffs it introduces.

Recent Trends in Military Spending

6. **Globally, military spending as a percentage of GDP halved between 1990 and 2008 compared to the Cold War period from 1970 to 1990.** The decline of military spending as a percentage of GDP and general government expenditure is consistent across all country groups: AEs, EMMIEs, and LICs (Figures 1A and 1B). All groups benefited from the peace dividend that followed the end of the Cold War. However, military expenditures have increased in recent years across all regions, particularly following Russia's war in Ukraine from 2022 onwards and the rising tensions in Asia and the Middle East. Military spending is shaped by both external and internal factors. External pressures include responses to international and/or regional conflicts and the influence of geopolitical tensions with neighboring countries. Internal pressures arise from domestic challenges such as political instability, violence, civil war, or terrorism. Collier (2006) also highlights factors like budgetary inertia during peacetime—that is, the tendency of military budgets to persist over time with little change, even when circumstances no longer justify the spending—and the role of vested interests.

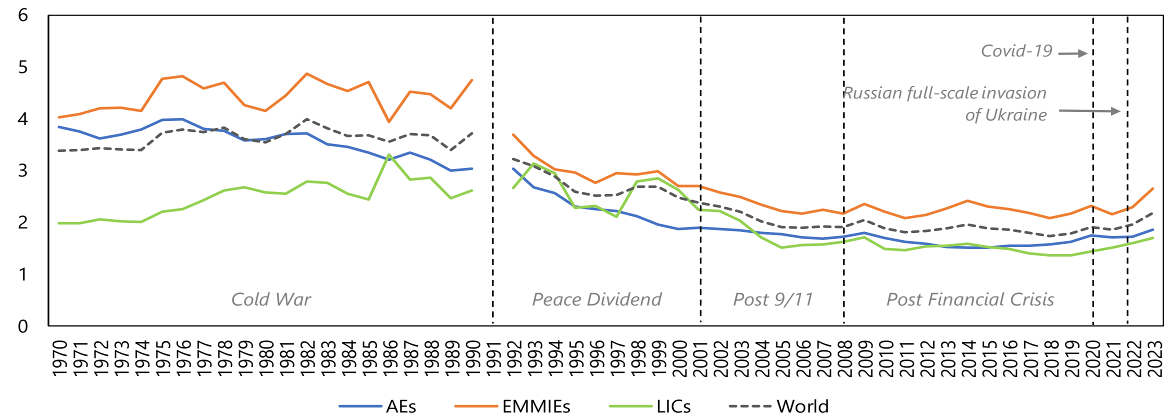
7. **Similar trends are seen in terms of the share of military spending in total budget outlays.** Across all country groups, the share of budgets allocated to the military has steadily declined since the 1980s but remains highest in FCS[2] at around 10 percent (Annex I). Currently, EMMIEs allocate an average of 8 percent of their budgets to the military, while AEs spend around 5 percent. Countries covered by the Fund's Middle East and Central Asia Department (MCD) allocate the largest share of both their GDP and total budget to military spending, while those covered by the Western Hemisphere Department (WHD) spend the least. The MCD region has consistently invested more in its military compared to other regions.

[2] In FY2024, 39 IMF member countries were considered FCS. Annex II lists the FCS for which staff discussed military spending in Article IV reports and/or program documents.

Figure 1. Military Expenditure

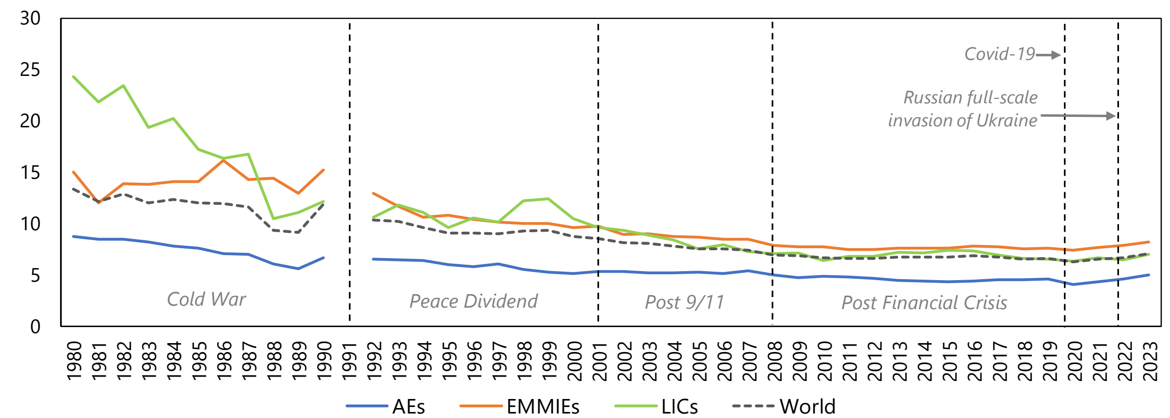
A. Military Expenditure as a Share of GDP, 1970–2023

(Average within country group, percentage of GDP)



B. Military Expenditure as a Share of Government Expenditure, 1980–23

(Average within country group, percentage of general government expenditure)



Source: IEO staff calculations based on SIPRI data.

Notes: AEs = Advanced Economies; EMMIEs = Emerging Markets and Middle-Income Economies; LICs = Low-Income Countries. Military expenditure calculated as the unweighted country average within each country group. Data for 1991 are not available due to the breakup of the former Soviet Union. The number of countries in the sample varies over time.

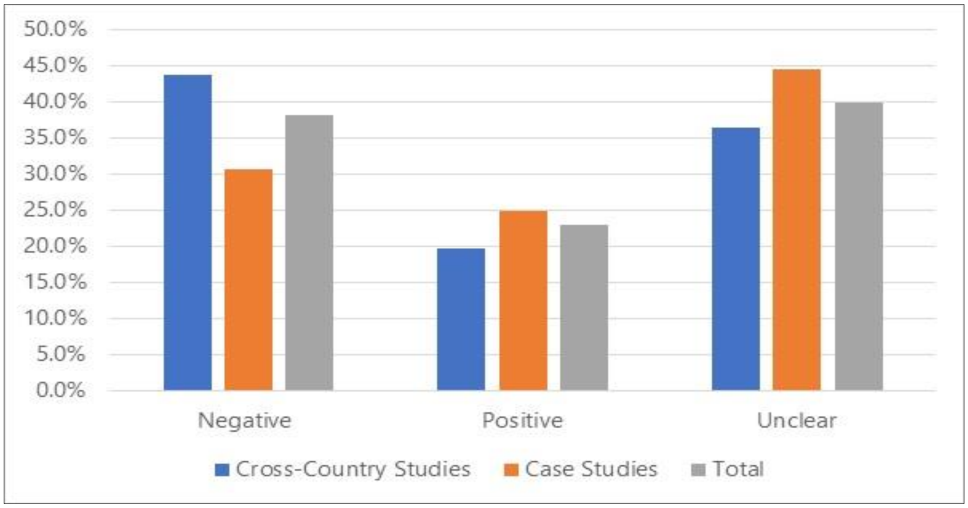
Impact on Growth

8. **The long-term effects of military spending on economic growth have been the subject of extensive debate.** Some scholars argue that military expenditure can stimulate growth by boosting demand and generating technological innovations, while others maintain it hampers growth by diverting resources from more productive sectors. Empirical findings are mixed. A literature review by Dunne and Tian (2013) concluded that most studies report a negligible or negative relationship between military spending and economic growth (Figure 2). Similarly, a meta-analysis by Alptekin and Levine (2012) finds a negligible effect in EMMIEs and LICs, but a positive effect in AEs. In a similar vein, d'Agostino and others (2017) examined the long-term relationship between military spending and economic growth across 83 countries from 1970 to 2014. Their findings indicate that a 1 percentage point increase in military spending

is associated, on average, with an 8.5 percent reduction in per capita GDP over a 20-year period. Ilzetzki (2025) finds that the short-term growth impact of military spending in the European Union depends on how the additional spending is financed—if funded through tax increases rather than public borrowing, the impact on GDP growth is likely to be smaller, or even negative. These findings hold regardless of whether the economy is in recession or experiencing a boom.

Figure 2. Longer-Term Impact of Military Spending on Economic Growth

(Percentage of studies)



Source: Dunne and Tian (2013).

Note: Based on a literature review of 96 cross-country studies and 72 case studies conducted since Benoit (1973) and 2013.

9. **Under certain conditions, military spending can foster growth and improve social welfare**. In FCS, increased military expenditures may yield short-term benefits by enhancing security and stabilizing socio-economic conditions. A notable example is Colombia, where the rise of the drug trade in the 1980s triggered escalating armed conflict and insecurity, with estimated economic costs at between 2 percent to 4.2 percent of GDP annually in the 1980s and 1990s (Giugale and others, 2002). Following the 2002 presidential election, the government launched a major military offensive against armed groups to curb insecurity, protect lives and property, and reestablish the state's monopoly on the use of force. As a result, military spending surged from an average of 2.3 percent of GDP per year (1975–2001) to 3.3 percent (2002–23) (SIPRI, 2025), contributing to a significant reduction in conflict and insecurity. In such cases, although large defense budgets are costly, they can yield important benefits by restoring law and order and lowering future risks of violence. However, over time, such spending can begin to crowd out more productive spending.

10. **The composition of military spending plays a critical role in influencing the growth impact of military spending**. Becker and Dunne (2023) show that the negative impact on economic growth of higher military spending is mainly attributable to personnel expenditures. In contrast, the adverse effects from operating and maintenance costs are minimal, and spending

on equipment and infrastructure has little measurable impact on growth. Military spending can also produce positive spillover effects through innovation. For example, Israel's Iron Dome missile defense system—developed through military R&D—has effectively protected civilian infrastructure and economic activity since its deployment in 2011 (Richemond-Barak and Feinberg, 2016). Many transformative technologies, including jet engines, computers, radar, nuclear power, semiconductors, GPS, and the internet, originated from military R&D. In the United States and several other Organisation for Economic Co-operation and Development (OECD) nations, defense-related R&D expenditures have historically surpassed other forms of public innovation funding. Using OECD data, Moretti and others (2019) found that increases in government-funded military R&D were linked to substantial growth in private sector R&D within the same firms or industries both within the country and across borders. Ilzetzki (2025) estimates long-run productivity gains of 0.25 percent associated with a temporary increase of 1 percent of GDP in military expenditure in North Atlantic Treaty Organization (NATO) and European Union countries, primarily through learning-by-doing and R&D.

11. **Structural factors can exacerbate the negative impact of military spending on growth, particularly in LICs**. Corruption can play a significant role in disproportionately allocating larger share of resources to the military, diverting funds from essential public services (Gupta and others, 2001). Weak institutions can further exacerbate inefficiencies and rent-seeking in military operations, raising the overall cost of military spending. LICs are also more vulnerable to terrorism than EMMIEs and AEs, where traditional civil wars have increasingly given way to non-state conflicts, such as terrorist attacks on civilians (Clements and others, 2020).

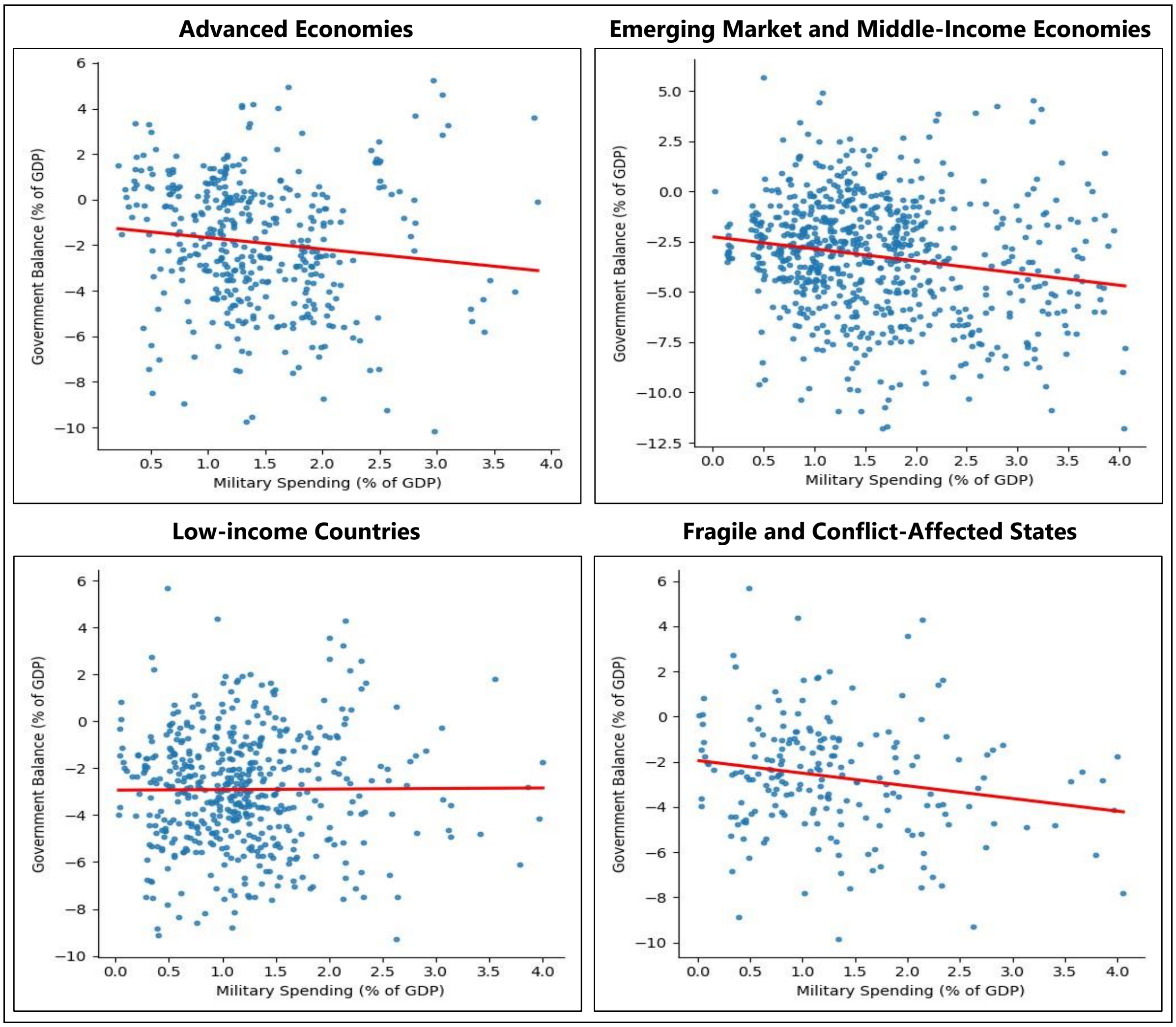
Fiscal Impact

12. **Higher military spending tends to be associated with higher fiscal deficits, but with a high degree of dispersion** (Figure 3). A similar relationship is found between military spending and debt, particularly in AEs and FCS (Annex III). This suggests that higher military expenditures reduce fiscal space, a crucial issue for FCS, which generally have the lowest revenue-to-GDP ratios (Baer and others, 2021). Developing countries are typically importers of arms due to the absence of a domestic arms industry. As a result, arms imports can have a significant impact on their balance of payments and national budgets, particularly in years when these imports occur. This often leads to greater volatility in defense budgets, which can, in turn, affect other areas of government spending and budget financing.

13. **High levels of military spending have also contributed to rising external debt, particularly in FCS in Sub-Saharan Africa** (Dunne and others, 2019). Although debt relief programs, including the Heavily Indebted Poor Countries Initiative and the Multilateral Debt Relief Initiative , significantly reduced the region’s debt by 2008, it has since increased partly due to renewed external borrowing, including for military spending. Conflict-induced fiscal pressures play a central role: declining fiscal balances and slower economic growth during conflict episodes drive up public debt. In Sub-Saharan Africa, intense conflict is associated with an average rise in the public-debt-to-GDP ratio of 16 percentage points within the first two years, with this increase

reaching nearly 20 percentage points by the fifth year. This has led to higher debt servicing costs, limiting the funds available for health, education, and infrastructure development (IMF, 2019a). As many of these conflicts persist and defense budgets continue to grow, ending violence could generate a substantial "peace dividend," enabling a reallocation of resources toward economic development and achieving the Sustainable Development Goals (Gupta and others, 2004).

Figure 3. Military Spending and Fiscal Balances, 2008–23



Source: IEO staff calculations based on SIPRI and WEO data.
Note: Every dot represents a single country in a single year.

14. **A high share of military spending in total government expenditure constrains fiscal space, often crowding-out other fiscal policy objectives, especially in middle and low-income countries.** Without enhanced domestic revenue mobilization and expenditure savings—such as through base broadening and improved tax administration and enhanced expenditure efficiency—higher military spending often comes at the expense of health, education, and infrastructure investment. In Sub-Saharan Africa, about a third of the countries have recently experienced a resurgence of conflict. IMF (2019a) shows that escalating conflict intensity—from no conflict to the

top quartile—is typically associated with a 12 percent decline in revenues (around 2 percent of GDP), a 9 percent rise in budgetary military spending (about 0.6 percent of GDP), and a decrease in capital expenditures of 9 percent. This reallocation reflects a shift from growth-enhancing investments to military spending. As a result, heightened conflict intensity is linked to a widening of the fiscal deficit by approximately 1.7 percent of GDP. This crowding out of productive spending is supported by evidence linking higher military expenditures with rising income inequality and weaker long-term growth prospects (Ali, 2007 and 2011; Gupta and others, 2004).

15. **Such crowding-out effects do not apply uniformly to AEs, which typically have not encountered the same financing constraints.** Some studies, such as Lin and others (2015) and Zhang and others (2017), even suggest a positive correlation between military and social spending in OECD and G-7 economies. However, the crowding out of social spending due to rising military expenditures is also likely to affect higher-income countries, many of which have increased their defense budgets in response to Russia's war in Ukraine. NATO countries—including Finland and Sweden, which recently joined the alliance—have committed to meeting or exceeding the 2 percent of GDP target for military spending by 2024 (from 1.43 percent of GDP in 2014), and to increase it to 5 percent by 2035 (Tian and others, 2024). Such increase will stress fiscal space available for other critical public investments, especially in contexts where the scope for additional taxation is limited and age-related spending is rising.

16. **Moreover, high military spending by neighboring countries can have adverse spillover effects, often perceived as security threats that prompt nations to increase their own defense budgets.** Research highlights the role of neighborhood effects and arms races in shaping military expenditures. Nearby conflicts, including civil wars, can impact the defense budgets of neighboring nations, regardless of the conflict state's own spending or whether the neighbor is directly involved (Collier, 2006; Phillips, 2014). Additionally, membership in military alliances, such as NATO, can exert pressure on countries to adjust their military expenditures. These alliances entail specific defense commitments while also offering collective security benefits (Clements and others, 2021).

III. IMF ADVICE ON MILITARY SPENDING

17. **The IMF's advice on military spending has largely been guided by the Executive Board Summing Up of the October 2, 1991, discussion** (IMF, 1991). The summing up was included in the list of Selected Decisions and Selected Documents of the Fund.[3] It clarifies that staff may engage with country authorities on military spending and its impact on a country's fiscal and external positions, as well as trade-offs, such as the macroeconomic effects of reduced military spending. Military expenditure may also be analyzed from a regional or global

[3] In that discussion, most Executive Directors indicated that military spending could have "*an important bearing on a member's fiscal policy and external position,*" emphasizing that "*national security, and judgments regarding the appropriate level of military expenditures... were a sovereign prerogative of national governments and were not in the domain of the work of the Fund*" (IMF, 1991).

perspective in the Fund's multilateral surveillance products. The 1991 Board decision further outlines the Fund's limitations in this area due to the sensitive nature of military spending: (i) the submission of data on military spending by country authorities is voluntary;[4] (ii) such data cannot serve as a basis for program conditionality; and (iii) the Fund must refrain from making judgements on the appropriate level of military spending.

18. **Further guidance was provided during the Executive Board discussion of the World Economic Outlook (WEO) in April 1994**. In that discussion, a background paper introduced the notion of unproductive public expenditures, defined as "*the difference between the actual public spending on the program and the reduced spending that would yield the same social benefit with maximum cost-effectiveness.*"[5] Applying this concept to military spending, it noted the spillover effects resulting from such expenditures, noting that "*military expenditure that is excessive—in the sense that the marginal improvement in national security associated with this expenditure is less than its economic cost—imposes burdens on both the spending country and other countries that believe their own security may be jeopardized by such expenditure*"[6] (IMF, 1994). Through the 1990s, Fund management emphasized the importance of improving the quality of government expenditures by reducing outlays for unproductive purposes, such as excessive military outlays not justified by national security needs.[7]

19. **The 1991 Board decision on military spending remains in effect and aligns with subsequent Board decisions on surveillance taken in 2007 and 2012.** Under these decisions, staff is required to discuss with country authorities, during annual surveillance, issues that are macro-critical, meaning those that can significantly influence present or prospective balance of payments or domestic stability (IMF, 2007; 2012). While the Fund's role in national security and military spending is limited, relatively high military spending can potentially have a significant impact on a country's fiscal situation and balance of payments. An important challenge for staff, however, is that there is no specific guidance—such as in the form of a guidance note—on how and when to cover military spending issues in practice. Staff is tasked with exercising discretion in prioritizing certain topics for more detailed analysis, adopting a risk-based approach, and drawing upon the expertise of other institutions where appropriate.[8]

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[4] Since the 1991 Board decision, annual data on military spending has been readily available from SIPRI, in line with standard fiscal reporting practices.

[5] The subsequent work on public expenditure efficiency at the Fund and elsewhere is consistent with the concept of unproductive spending. Studies have shown that countries expend 20–35 percent more resources in both education and health sectors to achieve similar goals as in more efficient countries (Gupta and Verhoeven, 2001; Herrera and Pang, 2005). Furthermore, developing countries lose over one-third of their public investment due to inefficient spending practices (IMF, 2015; Barhoumi and others, 2018).

[6] See also IMF (1995).

[7] See Camdessus (1991; 1998a; and 1998b).

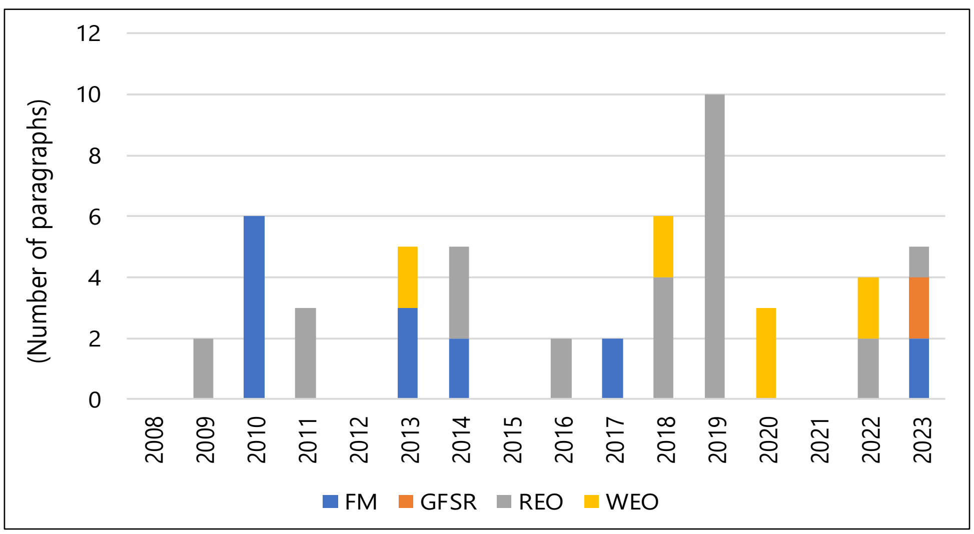
[8] See IEO (2025) for a discussion on what fiscal policy advice could cover and how.

20. **IMF staff have frequently used the terms "military spending," "security spending," and "defense spending" interchangeably in Article IV reports and program documents.** The term "government spending on security" is generally more acceptable to country authorities, as it emphasizes the role of security in enabling the economy to function effectively. In fact, around one-third of staff reports use the term "security spending."

Multilateral Advice

21. **Until recently, military spending received relatively limited coverage in IMF flagship reports, such as the WEO, the Fiscal Monitor, and the Global Financial Stability Report** (Figure 4).[9] This may be because global military spending as a percentage of GDP remained relatively stable throughout the review period, up until recently. The interest in military spending increased as a result of Russia's war in Ukraine and several flagship reports discussed military spending in 2022, 2023, 2024, and 2025. For example, both the April 2025 WEO and Fiscal Monitor highlight the fiscal challenges related to higher defense spending, particularly for countries with limited fiscal space. This aligns with the findings from bilateral surveillance discussed below. There have been occasional discussions in several Fiscal Monitors about the fiscal implications of changes in military expenditures—alongside other significant spending categories—in large AEs.

Figure 4. Coverage of Military Spending in IMF Flagship Reports, 2008–23



Source: IEO staff calculations based on FDET data.
Note: The figure displays the number of paragraphs that contain any of the following keywords: military spending, defense spending, security spending.

[9] This contrasts with the substantive discussions found in WEO reports from 1990 and 1993. In May 1990, there was a section on the impact of lower defense expenditures, followed by an annex in 1993 on the economic benefits of reducing military spending. These discussions reflected the breakup of the Soviet Union in 1990 and the resulting peace dividend. The then Managing Director, Michel Camdessus, was particularly interested in the topic.

22. **Military spending analysis has been relatively more prevalent in the Regional Economic Outlooks (REOs), particularly in the Sub-Saharan Africa outlook.** For instance, the April 2019 REO (IMF, 2019a) for Sub-Saharan Africa included a dedicated chapter to the economic impact, including their fiscal implications, of conflicts. In this region, a third of the countries have experienced conflict in recent years, particularly in the Sahel, which has impacted both their growth potential and the management of fiscal policy. However, the REO for MCD—the region with the highest military spending relative to its GDP—did not include any discussion of military expenditures or their macroeconomic implications during 2008–23.

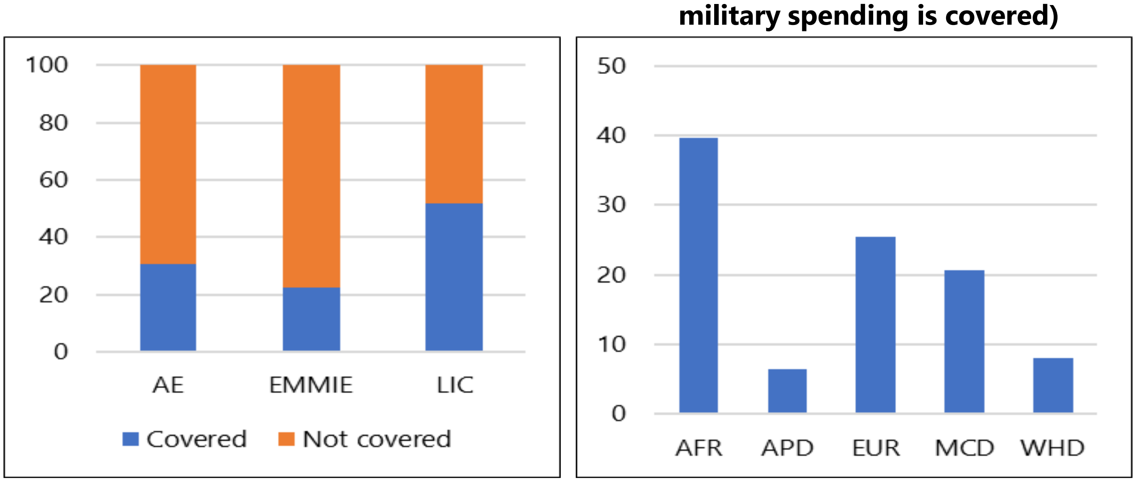
Bilateral Advice

23. **During the period under review, staff discussed military spending in Article IV reports and/or program documents for 63 countries, around one-third of the membership** (Annex II). The coverage of AEs was proportionate to their share in the Fund’s membership (Figure 5a). In contrast, LICs were covered more frequently relative to their share of membership, reflecting the inclusion of several FCS within the LICs. While FCS represented approximately 20 percent of the Fund's membership, they accounted for around 30 percent of countries where military spending was discussed in staff reports between 2008 and 2023. This outcome is not surprising, as FCS tend to allocate a larger share of their budget to the military, and there is a correlation between conflict and military spending. This underscores the macro-criticality of military spending in such contexts, unlike in countries where military spending is modest and less relevant to overall fiscal outcomes. Military spending was discussed across all five IMF area departments, with nearly 40 percent of the countries covered being in the African Department (AFR) (Figure 5.b). Notably, the discussion of military spending in country reports has grown in recent years.

Figure 5. Military Spending Coverage in Article IV Reports and Program Documents, 2008–23

A. Income Group (Percent of countries within each group)

B. Regional Distribution (Percent of all countries for which military spending is covered)



Source: IEO staff calculations based on Article IV reports and program documents.

24. **The coverage of military spending across the membership appears uneven**. For instance, the coverage of military spending in staff reports of countries with an above-average share of military spending in their budgets during 2008–23—combined with relatively high fiscal deficits and debt-to-GDP ratios—was inconsistent across the Fund's membership. Within this group, military spending was covered in countries such as Afghanistan, Chad, Niger, Iraq, Israel, Lithuania, Mali, Oman, and the United States. In contrast, in was not covered in countries such as Angola, Azerbaijan, Bahrain, Belarus, Iran, Lebanon, Morocco, Syria, South Sudan, and Yemen. This may reflect the reluctance of some national authorities and/or mission teams to address a topic considered sensitive, as well as the need to address other macro-critical issues like social spending and income inequality. Even when military spending as a share of the budget was below average, countries with a similar fiscal outlook received uneven treatment in Article IV reports. This discrepancy was particularly evident among European Union members. For instance, in Finland and Germany military spending was covered in Article IV reports, while in France, Portugal, Spain, and the United Kingdom, it was not.

25. **The depth of coverage was also uneven across countries with most cases—more than 70 percent—providing only limited references or a factual description of military spending trends.** Slightly less than 30 percent of the cases (24 countries) included discussions of macroeconomic trade-offs associated with military spending on one or more occasions. Trade-offs were discussed more frequently in AEs and EMMIEs than in LICs, with non-FCS LICs addressing them more than in FCS LICs, despite FCS typically facing tighter fiscal constraints and allocating a larger share of their budget to the military. For instance, in countries like Germany and Israel, Fund staff discussed macroeconomic trade-offs associated with military spending in their surveillance reports, but such discussions were absent in reports on Myanmar and Russia. Using a scalar rating system of 1, 2, and 3 for limited references (signaling), factual descriptions, and macroeconomic trade-off analysis in Fund documents, respectively, and consolidating these into a single score, Figure 6 illustrates the unevenness of analysis on military spending.

26. **The IMF has raised concerns about the use of off-budget mechanisms to finance military spending.** Transparency issues arise when military spending is financed through off-budget mechanisms and excluded from the scope of Article IV consultations. For instance, in Germany, the Fund noted the extensive use of extrabudgetary funds, including for defense, which could undermine the credibility of the fiscal framework over time and advised to provide a consolidated report on fiscal risks, encompassing all contingent liabilities to enhance fiscal transparency and improve risk management (IMF, 2023b). In Israel, the Fund recommended that grants from the United States and related defense spending be reported in the budget (IMF, 2022). In Russia, the share of spending classified as secret for national security purposes

increased between 2013 and 2018. The Fund's Fiscal Transparency Evaluation (FTE)[10] indicated that the secret allocations were directed toward border protection, armaments, and national security. The most recent Article IV report for Russia (2020) recommended that the authorities refrain from engaging in quasi-fiscal activities through sovereign wealth funds.

Figure 6. Depth of Military Expenditure Coverage in Article IV Reports and Program Documents, 2008–23

Source: IEO staff calculations based on Article IV reports and program documents.
Note: The depth analysis is based on three considerations: references to military spending in staff papers, factual description of military expenditures, and the discussion of macroeconomic trade-offs between military spending and other key variables.

27. **The advice on military spending in an IMF-supported program depended on the specific circumstances of each country, including whether the country was facing an ongoing conflict**. For instance, in Ukraine, Fund-supported programs recognized the need to accommodate high military spending within macroeconomic targets. In 2014, this was highlighted as a challenge to meet program targets, given significant impacts on capital flows and international reserves. By 2015, the focus shifted to improving the budget composition by reducing inefficient spending to achieve savings—a strategy further pursued in 2018. Following Russia's war in Ukraine from 2022 onwards, the program acknowledged that Ukraine would need to finance its fiscal deficit largely through external support, as measures like cutting subsidies and

[10] The Fund conducts FTEs to assess whether a country's fiscal management of revenues and expenditures is transparent and meets the standards set in the code of fiscal transparency. To date, FTEs have been conducted in 37 countries that requested them, with several countries requesting updates, but only a handful of them have addressed military or security-related spending. The FTE for Russia noted that in 2013, 14 percent of total expenditure was classified as secret, rising to 17 percent in 2018 (IMF, 2019b). The Turkish FTE reported an extrabudgetary fund, the Defense Industry Support Fund, amounting to 0.19 percent of GDP, which was allocated to support the military (IMF, 2017). In Jordan, the wage bill is approximately 50 percent of total current expenditures, whereas fiscal reports only identify around 20 percent in current spending, as military spending is excluded (IMF, 2021).

reducing tax exemptions would not suffice to create room for increased military spending (see also Box 1). In contrast, the approach in Georgia and Greece was to curtail high military spending to strengthen macroeconomic balances. During Greece's 2010 and 2012 programs, fiscal consolidation efforts included reducing the wage bill and rationalizing defense spending to align with the OECD levels, while also aiming to achieve efficiency gains in government operations at both central and local levels. Similarly, Georgia's 2008 Fund-supported program aimed at lowering import-intensive military spending to align with levels seen in comparable countries.

Box 1. Military Spending in Ukraine Since 2022

In February 2022, Russia launched a full-scale invasion of Ukraine, prompting Ukraine to rapidly increase its military expenditures and seek urgent financial assistance, including from the Fund. The Fund reacted quickly, providing substantial financial support. However, this required changes to its traditional lending framework, as Ukraine could not fulfil some of the standard requirements for Fund financing.

Given the challenges of conducting a debt sustainability assessment without a medium-term economic forecast, the Fund initially extended emergency support through the Rapid Financing Instrument (RFI). On March 9, 2022, the Board approved a disbursement of USD 1.4 billion, followed by an additional USD 1.3 billion on October 7, 2022, under the RFI's food shock window. On December 19, 2022, the Board endorsed a four-month Program Monitoring with Board involvement (PMB) designed to maintain macroeconomic stability and catalyze donor support amidst considerable risks. Following Ukraine's success with the PMB, the Fund revised its lending framework in March 2023 to allow financing for countries experiencing "exceptionally high uncertainty" due to external shocks beyond their control, without lowering the upper credit tranche (UCT) quality of Fund-supported programs.[1] This policy shift enabled the approval of a 48-month Extended Fund Facility (EFF) for Ukraine on March 31, amounting to approximately USD 15.6 billion. The EFF formed part of a comprehensive USD 115 billion international support package aimed at ensuring economic stability, restoring debt sustainability, and fostering reforms for post-war recovery. This policy shift not only enabled continued support for Ukraine but also set a precedent for future lending to other Fund members facing similar circumstances, with Ukraine as a pilot for the new framework.

Since the onset of the war, Fund staff reports have underscored the difficult tradeoffs facing Ukraine regarding military spending. The conflict has driven a sharp increase in the fiscal deficit, fueled by elevated defense expenditures, financed through external support and monetary measures. This, in turn, has resulted in soaring public debt and a loss of market access. The war necessitated prioritizing defense and social protection, resulting in multiple supplementary budgets and a marked reduction in non-priority spending. While the budget for 2023 was supported by strong external financing commitments, the increased defense spending contributed to missed targets for overall budget balance and social spending.

Sources: Betliy (2023); IMF (2023a); various press releases/staff reports for Ukraine (2022–23).

[1] Two reforms to the Fund's financing assurances policy enabled the Fund to do so: (i) allowing upfront commitment to debt relief with a contingent second-stage element; and (ii) extending the use of a capacity-to-repay assurance from official bilateral creditors/donors from emergency financing to a UCT context (IMF, 2023a).

28. **Within program countries, some authorities have raised concerns about perceptions of lack of evenhandedness.** Notably, authorities in FCS countries under a Fund program expressed concern that Fund policy advice did not adequately prioritize restoring and maintaining security. They emphasized that security is paramount to ensure stability and fostering economic development and must take precedence over other priorities, whereas staff focused mostly on debt sustainability and fiscal adjustments. In this respect, they pointed to a more accommodating

treatment of military spending in the case of Ukraine.[11] Staff argued that they considered security concerns and the need for military spending. They also noted that their advice was tailored to country-specific circumstances, including funding constraints and risk of debt distress. In the absence of adequate external support, sustaining high levels of military spending often required cuts in other current expenditures, including wages and subsidies (see also Box 2).

29. **More generally, recent increases in military spending, including in AEs, further underscore the need for a pragmatic and context-sensitive approach to security-related spending.** Following Russia's war in Ukraine, extra-budgetary military spending has expanded, including in AEs, leading to various financing strategies such as Poland's use of debt bonds, Denmark's reduction of national holidays, the UK's budgetary adjustments reducing Overseas Development Assistance (ODA) to finance the increase in defense spending,[12] or Germany's 2022 EUR 100 billion special fund in 2022 to modernize and acquire new weapon systems (Cameron, 2024).[13] The increase in military spending is also being accommodated through reforms or added flexibility in implementing fiscal rules (Pench, 2025; Tuma, 2025). For instance, the recent White Paper on European Defense and the ReArm Europe Plan/Readiness 2030, recommends activating the national escape clause of the Stability and Growth Pact (SGP), allowing member states to increase defense expenditures without invoking the excessive deficit procedure (EDP) (European Commission, 2025). Germany has also reformed its "Debt Brake" fiscal rule to increase military spending and stimulate economic growth through infrastructure investments.[14]

[11] The revision of the lending framework to allow financing for countries experiencing "exceptionally high uncertainty" due to external shocks beyond their control (see also Box 1 and 2) is applicable to all IMF members; however, this policy change occurred in 2023 and therefore cannot be factored into comparisons with previous years.

[12] On February 25, 2025, the United Kingdom government announced plans to raise defense spending by 0.2 percentage points, increasing it to 2.5 percent of GDP starting in April 2027, with a goal of reaching 3 percent in the following parliamentary term, and financing this increase by reducing ODA from 0.5 percent to 0.3 percent of GNI (Prime Minister's Office, 2025).

[13] Other examples include the use of revenues from copper exports in Chile to fund part of its military budget (based on a 1958 law)—in 2019, military financing was set to transition to being funded through the national budget by 2029 ending the reliance on off-budget allocations while maintaining spending on arms procurement as classified (Lopes da Silva and Tian, 2019). Between 2010 and 2019, Egypt acquired a significant number of new arms despite official data indicating a decline in military spending compared to the previous decade, suggesting off-budget resources (Kuimova, 2020).

[14] The reform allows military expenditures exceeding 1 percent of GDP to bypass borrowing limits and establishes a EUR 500 billion infrastructure fund. This reform was deemed essential because the European Commission's proposal to activate the national escape clause, which would permit the exclusion of up to 1.5 percent of GDP in military spending from the fiscal rules, would not have permitted Germany to finance its broader infrastructure agenda (Marsh and Williams, 2025; Pench, 2025).

Box 2. Advice on Military Spending in Fragile and Conflict-Affected States with an IMF Program

The Fund paid particular attention to FCS in its discussions on military spending. Addressing military spending in FCS contexts can be especially challenging due to data gaps, weak expenditure classification systems, and heightened political sensitivity surrounding such expenditures. Among FCS, the Sahel region has seen a significant rise in conflict since 2000, with a marked escalation after 2010. All six Sahel countries, except Nigeria, had substantial program engagement with the Fund. Military spending was addressed in staff reports for all of them; however, discussions were notably less frequent for **Nigeria**, which was only subject to surveillance.

In **Burkina Faso**, staff noted in 2016 that economic growth was depressed by the diversion of productive public investment to security-related expenditures. By 2018, the authorities committed to maintaining a fiscal deficit of 3 percent of GDP, bolstered by windfall revenues. However, the Fund cautioned against relying on one-off revenues for permanent expenditures and emphasized the necessity of broadening the tax base, improving tax administration, and enhancing expenditure efficiency to create sustainable fiscal space for military and other essential spending.

In **Cameroon**, by 2017, fiscal consolidation efforts fell short, as urgent security expenditures and infrastructure spending pushed the budget deficit to 5 percent of GDP, exceeding the target of 3.1 percent. In 2021, although program implementation was deemed satisfactory, concerns remained about controlling security-related expenditures and reliance on exceptional spending procedures. The authorities took steps to improve monitoring and reduce unnecessary expenditure, reflecting the ongoing difficulty of balancing military spending with fiscal discipline amid challenging economic conditions.

In **Chad**, staff emphasized the need for fiscal sustainability amid rising non-oil primary fiscal deficits. In 2008, the Fund recommended a medium-term fiscal adjustment path to align permanent expenditures with non-oil revenues, urging the government to increase non-oil revenue collection and strengthen public financial management. Security spending surged from 2.25 percent of GDP in 2005 to nearly 14.5 percent in 2008, significantly widening fiscal deficits. This expenditure was often unpredictable and exempt from budget scrutiny. By 2014, while the authorities committed to expenditure cuts, security spending was excluded from fiscal constraints due to regional instability. The deteriorating security situation further necessitated increased military spending in subsequent years, illustrating the ongoing tension between maintaining fiscal discipline and addressing urgent security needs.

In **Mali**, staff discussed the ongoing challenge of achieving fiscal consolidation while addressing urgent security needs. In 2013, the authorities committed to adhering to the WAEMU's fiscal deficit target of 3 percent of GDP by 2019 and prepared a medium-term military spending plan, with intentions to improve tax collection and reduce non-priority spending if necessary. In 2018, Mali managed to maintain a fiscal deficit of approximately 2.9 percent of GDP, even as military expenditures rose significantly. However, in 2023, the impact of ECOWAS sanctions caused a 17 percent revenue drop, prompting prioritization of essential expenditures, including military, suggesting that any deterioration in the security situation could further restrict funding for development projects.

In **Niger**, the focus in 2008 was on promoting economic growth while maintaining fiscal discipline, with a modest increase in security expenditures anticipated to be contained in the future. By 2012, the growing security threats prompted greater concern about the balance between fiscal sustainability and defense needs. The Fund called for enhanced revenue mobilization, tighter spending control, and stronger public financial management to reduce fiscal deficits. In 2017, declining revenues coupled with increased security spending posed significant fiscal risks, though key debt indicators remained within thresholds. Overall, the Fund emphasized the necessity of careful management of military expenditures to ensure broader economic stability and fiscal health.

Sources: De Lannoy and Lane (2025); IEO (2018); IMF (2019a); Staff Reports for Burkina Faso, Cameroon, Chad, Mali, Niger, and Nigeria (2008–23); interviews with Executive Board members and staff.

IV. Assessment and Suggestions for Next Steps

30. This section categorizes lessons learned regarding military spending in the Fund's fiscal policy advice according to three evaluation criteria: consistency, relevance, and evenhandedness.

Consistency

31. **This chapter finds that the IMF's treatment of military spending in fiscal policy advice aligns with its mandate and Executive Board decisions.** The Fund's approach to military spending is shaped by its 1991 Executive Board Summing Up, which emphasized its fiscal and balance of payments implications for member countries. This guidance is also consistent with later Board decisions on surveillance, particularly those made in 2007 and 2012. The policy advice related to military spending in Article IV reports and/or program documents concentrated on its fiscal implications and influence on balance of payments or domestic stability, without making assumptions about national security concerns or the appropriate level of military expenditures, which remain the sovereign prerogative of national governments. In its multilateral surveillance, coverage of military spending in the Fund's flagship reports was limited to its macroeconomic effects, either from a global or a regional perspective.

Relevance

32. **Military spending becomes macro-critical when it significantly affects fiscal policy and balance of payments.** After a global decline in the post-Cold War era, recent conflicts and geopolitical shifts—most notably Russia's war in Ukraine—have led to a resurgence in military spending. Elevated military expenditures can exacerbate fiscal deficits, increase public debt, and crowd out critical investments in healthcare, education, and infrastructure. This erosion of fiscal space threatens economic growth, and the achievement of the Sustainable Development Goals, potentially destabilizing balance of payments and domestic stability.

33. **Despite its macroeconomic importance, military spending received relatively limited attention in IMF flagship reports, Article IV reports, and program documents between 2008 and 2023.** While attention to military spending started picking up towards the end of the evaluation period, before 2022, only the sub-Saharan Africa REO provided an in-depth discussion on military spending, particularly in the context of rising conflicts in the Sahel region. Article IV reports and program documents for 63 countries, or around one-third of the membership, mentioned military spending, and of those, slightly less than 30 percent discussed the macroeconomic trade-offs. In AEs, rising military spending in the later part of the evaluation period did not appear to have influenced the Fund's bilateral policy advice, which remained broadly unchanged. Most references were either brief mentions or factual descriptions of spending trends, offering limited value in terms of fiscal guidance.

Evenhandedness

34. **It is unclear why IMF staff explicitly discussed military spending in some countries with above-average military spending in the budget, combined with high fiscal deficits and debt-to-GDP ratios, but not in others with similar or even more constrained fiscal conditions.** In some instances, countries with below-average military spending received more attention than those with higher levels, leading to inconsistencies in treatment across staff reports. Over time, successive surveillance decisions, reviews, and guidance notes have widened the scope of the Fund's policy advice—both in terms of range of issues and the time horizon considered. As a result, country teams have considerable discretion to prioritize issues they deem most important. Also, some authorities are hesitant to discuss military spending explicitly and prefer to frame discussion in broader terms, such as overall fiscal balances or fiscal pressures.

35. **When military spending was addressed, the IMF's treatment varied significantly across countries, largely reflecting country-specific circumstances, including financing constraints and debt sustainability concerns**. Additionally, a policy change implemented in March 2023, which permits Fund lending to countries facing "exceptionally high uncertainty" due to external shocks beyond their control, complicates comparisons between Ukraine and earlier cases. While this policy shift is expected to benefit other Fund members in similar situations, it falls outside the scope of this evaluation since it occurred at the end of the evaluation period.

Possible Ways Forward

36. **To enhance the consistency, relevance, and evenhandedness of its coverage of military spending in fiscal policy advice, the IMF could consider the following suggestions aligned with the 1991 Board decision:**

- **Unifying terminology.** The Fund should consider consistently using the term "military spending" in its documents, in line with the 1991 Board decision on military spending. When using other terms, such as "security spending," staff should consider clarifying whether it includes spending other than military spending (like for example, outlays on regular police operations).

- **Scaling up analysis of military spending in flagship publications.** In the current context of rising global expenditures in military spending, key Fund reports, such as the WEO, the FM, and REOs could discuss their macroeconomic implications, similar to how the WEO once examined the "peace dividend" after the breakup of the Soviet Union in the 1990s.

- **Enhance the consistency of military spending advice across countries.** While discussions on military spending must be context-specific, and staff should retain discretion in determining when selected macroeconomic topics are deemed macro-critical, there is scope for a more even treatment of military expenditures across the membership, especially for countries with comparable fiscal conditions and military expenditure patterns. The ongoing 2026 CSR presents an opportunity to revisit the issue of military spending in the context of surveillance.

- **Incorporate off-budget military spending into debt sustainability analysis.** Military expenditure outside the official budget could be explicitly incorporated into debt sustainability frameworks, particularly when such spending is substantial and/or when arms imports constitute a significant share of total spending. This would improve understanding of underlying drivers of debt accumulation and help identify cases where defense spending contributes to rising debt levels, potentially threatening long-term fiscal sustainability and posing risks to balance of payments stability.

ANNEX I. MILITARY EXPENDITURE

Table AI.1. Military Expenditure: Summary Statistics, 1970–2023

	As Percent of GDP						As Percent of General Government Expenditure					
	1970–1990	1992–2000	2001–2009	2010–2019	2020–2021	2022–2023	1980–1990	1992–2000	2001–2009	2010–2019	2020–2021	2022–2023
World												
Mean	3.63	2.74	2.06	1.84	1.88	2.07	11.48	9.33	7.65	6.69	6.43	6.89
St. Dev.	(3.79)	(3.04)	(1.74)	(1.51)	(1.36)	(2.80)	(9.11)	(7.65)	(6.22)	(5.71)	(5.16)	(6.80)
AEs												
Mean	3.56	2.33	1.79	1.58	1.73	1.79	7.27	5.85	5.19	4.57	4.21	4.80
St. Dev.	(3.79)	(1.86)	(1.14)	(1.00)	(0.94)	(0.93)	(5.87)	(5.96)	(5.35)	(4.77)	(3.10)	(3.61)
EMMIEs												
Mean	4.44	3.02	2.36	2.21	2.24	2.48	14.44	10.52	8.62	7.62	7.53	8.07
St. Dev.	(4.40)	(2.74)	(1.65)	(1.81)	(1.69)	(3.91)	(8.72)	(6.99)	(6.22)	(5.95)	(6.09)	(8.77)
LICs												
Mean	2.50	2.64	1.80	1.48	1.47	1.65	16.09	10.99	8.12	6.93	6.52	6.75
St. Dev.	(2.16)	(4.05)	(2.17)	(1.12)	(0.86)	(1.21)	(10.93)	(9.07)	(6.35)	(5.59)	(4.39)	(4.70)
FCS												
Mean	3.99	3.60	2.62	2.07	1.80	3.22	21.77	13.94	10.14	8.82	8.10	9.74
St. Dev.	(3.84)	(4.90)	(2.78)	(1.77)	(1.08)	(6.23)	(13.84)	(10.66)	(7.78)	(6.88)	(5.01)	(10.00)
AFR												
Mean	2.61	2.73	1.80	1.55	1.55	1.63	15.26	9.25	7.43	6.49	6.13	6.29
St. Dev.	(2.28)	(4.44)	(2.20)	(1.17)	(0.87)	(1.15)	(10.68)	(8.26)	(5.80)	(4.30)	(3.38)	(3.77)
APD												
Mean	2.91	2.54	1.80	1.68	1.74	1.62	11.10	10.58	8.31	7.46	6.59	6.83
St. Dev.	(1.73)	(1.55)	(1.01)	(0.81)	(0.87)	(0.86)	(7.44)	(6.44)	(5.91)	(5.36)	(3.92)	(4.94)
EUR												
Mean	3.56	2.31	1.78	1.51	1.70	2.48	6.44	4.75	4.95	4.32	4.58	6.42
St. Dev.	(3.98)	(1.78)	(1.05)	(0.96)	(0.97)	(4.71)	(3.67)	(3.44)	(4.87)	(5.23)	(5.69)	(10.07)
MCD												
Mean	7.47	4.55	3.61	3.65	3.53	3.57	21.03	16.57	13.33	12.32	12.13	11.94
St. Dev.	(5.94)	(3.51)	(2.02)	(2.35)	(2.15)	(2.03)	(9.35)	(8.39)	(6.82)	(6.89)	(5.76)	(6.15)
WHD												
Mean	2.62	1.62	1.43	1.35	1.35	1.19	13.31	6.65	5.39	4.63	4.24	4.12
St. Dev.	(1.76)	(0.92)	(0.98)	(0.91)	(0.85)	(0.78)	(10.19)	(3.77)	(3.35)	(2.62)	(2.12)	(2.12)

Source: IEO staff calculations based on the SIPRI and WEO data.
Note: AE = Advanced Economies, AFR = African Department; APD = Asia and Pacific Department; EMMIEs = Emerging Markets and Middle-Income Economies; EUR = European Department; LICs = Low-Income Countries; MCD = Middle East and Central Asia Department; WHD = Western Hemisphere Department.
Data for 1991 are not available due to the breakup of the former Soviet Union. The number of countries in the sample varies over time.

ANNEX II. COVERAGE OF MILITARY SPENDING

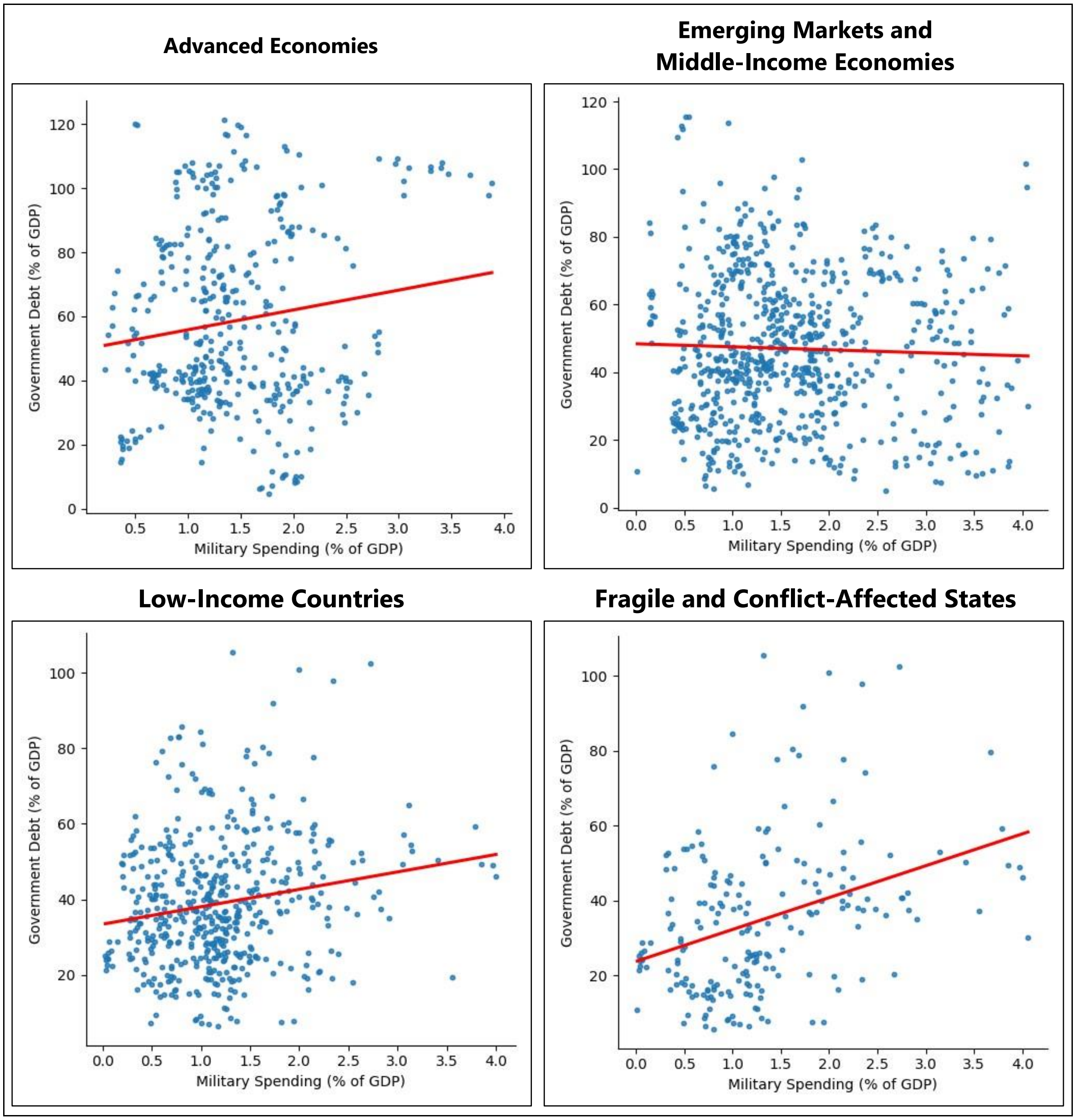
Table AII.1. Countries for Which the Fund Covered Military Spending in Article IV Reports and/or Program Documents, 2008–23

Advanced Economies	Emerging Market and Middle-Income Economies	Low-Income Economies
APD	**AFR**	**AFR**
Singapore	Eswatini	Benin
	Seychelles	Burkina Faso (FCS)
EUR		Burundi (FCS)
Denmark	**APD**	Cameroon (FCS)
Estonia	Sri Lanka	Central African Republic (FCS)
Finland		Chad (FCS)
Germany	**EUR**	Congo, Dem. Rep. of the (FCS)
Greece	Bulgaria	Congo, Rep. of (FCS)
Israel	Poland	Côte d’Ivoire
Latvia	Romania	Eritrea (FCS)
Lithuania	Russia	Ethiopia
Norway	Turkey	Gambia, The
Switzerland	Ukraine (FCS)	Guinea
		Guinea-Bissau (FCS)
WHD	**MCD**	Kenya
United States	Armenia	Liberia
	Georgia	Malawi
	Iraq (FCS)	Mali (FCS)
	Jordan	Mozambique (FCS)
	Oman	Niger (FCS)
	Pakistan	Nigeria (FCS)
	Saudi Arabia	Senegal
	Tunisia	Uganda
		APD
		Cambodia
		Myanmar (FCS)
		MCD
		Afghanistan (FCS)
		Djibouti
		Mauritania
		Somalia (FCS)
		Sudan (FCS)

Source: Text analysis based on Article IV reports and program documents. For FCS designation: https://www.imf.org/-/media/Files/Publications/PP/2023/English/PPEA2023010-S002.ashx.

ANNEX III. MILITARY SPENDING AND GENERAL GOVERNMENT GROSS DEBT

Figure AIII.1. Military Spending and General Government Gross Debt, 2008–23
(Percent of GDP)



Source: IEO staff calculations based on SIPRI and WEO data.
Note: Every dot represents a single country in a single year.

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