THE IMF RESPONSE TO THE GLOBAL CRISIS

Lecture 7

LIUC 2009

IMF response to the crisis

As the world economy has been hit by the worst crisis in many generations, the IMF has mobilized on many fronts to support its member countries by:

1. **Tripling its resources**
2. **Stepping up crisis lending**
3. **Providing analysis and targeted advice**
4. **Becoming more flexible**
5. **Reforming its governance**

1. Tripling the IMF resources

- At the G-20 Summit on April 2, 2009 the world leaders pledged to support growth in emerging market and developing countries by tripling the IMF's lending capacity to **$750 billion**. They committed to:
  - ✓ **increase the resources available by $250 billion** through immediate contributions that would subsequently be incorporated in the ***New Arrangements to Borrow*** (NAB) credit line. The G-20's intention is to increase the resources available through a more flexible NAB by **up to $500 billion**.
  - ✓ support a **general allocation of the IMF's Special Drawing Rights** equivalent to **$250 billion** to boost global liquidity**.**
  - ✓ **use additional resources from agreed sales of IMF gold to provide $6 billion** in additional financing for poor countries

IMF Borrowing Arrangements

- The **General Arrangements to Borrow** (**GAB**) and the **New Arrangements to Borrow** (**NAB**), are credit arrangements between the IMF and a group of members and institutions to provide supplementary resources to the IMF to deal with exceptional situations that poses a threat to the stability of that system. The maximum amount of resources available under the NAB and GAB is **SDR 34 billion**.
- As of end-July 2009, three *bilateral borrowing agreements*, designed to temporarily bolster the Fund's resources during the current crisis, were effective: **Japan** ($100 billion), **Norway** ($4.5 billion), and **Canada** ($10 billion).
- In addition, **EU** members have pledged loans worth €75 billion. **Switzerland** has pledged about $10 billion. **China**, **Brazil** and **Russia** have indicated their willingness to invest in notes issued by the IMF.
- The G-20 agreed that these bilateral contributions will subsequently be incorporated into the NAB.

Special Drawing Rigths, SDRs

- The SDR is an international reserve asset, created by the IMF in 1969 to supplement its member countries' official reserves. Its value is based on a basket of four key international currencies
- The IMF may allocate SDRs to members in proportion to their IMF quotas. *Such an allocation provides each member with a costless asset.*

Special Drawing Rigths, SDRs (cont.)

- There are two kinds of allocations of SDRs:
  - ✓ **General allocations** To be based on a long-term global need to supplement existing reserve assets.
  - ✓ **Special allocations** to enable all members of the IMF to participate in the SDR system on an equitable basis and correct for the fact that some countries had never received an SDR allocation.
- With a general SDR allocation taking effect on August 28 and a special allocation on September 9, 2009, the amount of SDRs increased **from SDR 21.4 billion to SDR 204.1 billion** (currently equivalent to about $317 billion).

Gold sales

- The IMF holds 103.4 million ounces (3,217 metric tons) of gold, making it the third largest official holder of gold. The gold is valued on its balance sheet at SDR 5.9 billion on the basis of historical cost.
- In September 09 the Executive Board approved the sale of a limited portion (about one-eighth) of the Fund's total gold holdings

2. Stepping up crisis lending

- The objective is to at least **double concessional lending for low-income countries**. Up to $17 billion has been made available to help low-income countries over five years and zero interest rates on outstanding IMF concessional loans through end-2011
- A new **flexible credit line have been created** for countries with very strong fundamentals, policies, and track records of policy implementation.
- **Normal access limits for countries are being doubled**. The new annual and cumulative access limits to non concessional lending are 200 and 600 percent of quota, respectively. Still scope for higher access under intensified scrutiny by the IMF's Executive Board.
- Lending commitments have reached a record level of **SDR 109 billion** *(as of Sept. 2009)*.

3. Providing analysis and targeted advice

- To shape the post-crisis world and try to prevent future crises, the IMF is closely working with governments and other international institutions.
- Steps undertaken to: enhancing risk analysis, taking a cross-country perspective, examining linkages between the real economy and the financial sector and external stability, developing an early-warning exercise (jointly with the Financial Stability Board), revamping the Financial Sector Assessment Programs.
- More attention to the effectiveness of country surveillance
- Advice on how to revamp global regulation and supervision of markets
- Drawing lessons from the crisis for policy, regulation, and reform of the global financial architecture

4. Becoming more flexible

The IMF has overhauled its general lending framework to make it better suited to country needs and streamlined conditions attached to loans. The lending toolkit has been simplified and some facilities eliminated

- **Cost and maturity structures have been simplified** to create the right incentives for borrowing from the Fund
- A new **flexible credit line** for strong-performing economies has been introduced
- Away with “hard” structural **conditionality**, new focus on objectives rather than specific actions

5. Reforming IMF governance

Why a change in governance was needed?

‘…The governance of the IMF should evolve along with the world economy, so that countries have a rightful stake in the institution. The world economy has evolved considerably, as some countries have grown more quickly than others and Europe has achieved monetary union and deepened integration.’

(*Timothy D. Adams, US Department of the Treasury*, 23 September 2005)

Quota misalignments

	Actual	Calculated
Advanced economies	60.5	65.0
Major advanced economies	45.2	45.4
Of which: US	17.1	16.0
Other advanced economies	15.3	19.6
Developing countries	32.1	29.6
Africa	5.4	2.3
Asia 7/	11.5	17.5
Middle East, Malta & Turkey	7.6	4.8
Western Hemisphere	7.6	5.0
Transition economies	7.4	5.5
Total	100.0	100.0

IMF: Quota –Updates Calculations July 07 (data 2005)

Reasons for reform

- **IMF governance** did not reflect individual country's position in the global economy.
- **Requests**:
  - ✓ Asian countries: increase their **quota** and their voting power;
  - ✓ Developing countries: increase their **voice** in the institution (quota is just one aspect of the problem).

The resolution adopted in Singapore

- In September 2006, the Board of Governors adopted a Resolution aimed at better aligning the IMF members' quota shares with their positions in the world economy, enhancing the voice of low-income countries.
- The reform program had the following elements:
  - ✓ ad hoc quota increases for a group of underrepresented countries: China, Korea, Mexico, Turkey
  - ✓ a simpler and more transparent quota formula, to be completed within the 2008 Annual Meetings
  - ✓ a second round of ad hoc quota increases, based on the new formula
  - ✓ an increase in basic votes

April 2008 Reform

- On April 28, 2008, a large-scale **quota and voice reform** was adopted.
- The reform builds on an initial step agreed in September 2006 but the reform package is more far-reaching, containing the following elements:
  - ✓ A new quota formula.
  - ✓ Ad-hoc quota increases to all 54 countries that were underrepresented under the new quota formula.
  - ✓ Tripling the number of basic votes to increase the voice of low-income countries .
  - ✓ Providing resources for an additional Alternate Executive Director for the two African chairs represented on the IMF's Executive Board.
  - ✓ Realigning quota and voting shares every five years.

New quota formula

- The newly agreed quota formula is a weighted average of GDP (weight of 50 percent), openness (30 percent), economic variability (15 percent), and international reserves (5 percent).

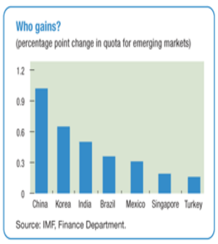
Calculated Quota Share (CQS) = (0.5*Y+0.3*O+0.15*V+0.05*R)^K

Y = GDP
O = annual average of the sum of current payments and current receipts for a five year period
V = variability of current receipts and net capital flows
R = official reserves
K = a compression factor of 0.95

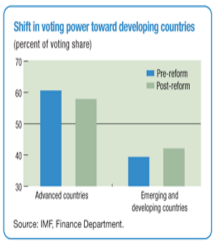
The outcome of the 2008 quota reform

- 135 countries increase their voting power, with an aggregate shift of 5.4 percentage points
- A total of 54 countries increase their nominal quotas ranging from 12 to 106%, with aggregate quota shares for these countries increasing by 4.9 percentage points.
- Consistent with the objectives of the reform, some of the largest increases go to dynamic emerging market countries.

Who gains?



Source: IMF, Finance Department.



Source: IMF, Finance Department.

What's next?

- Governance reform is currently being accelerated.
- In April 2009, the IMFC called for a prompt start to the **Fourteenth General Review of Quotas** so that it is completed by January 2011—some two years ahead of the original schedule. It is expected to result in increases in the quota shares of emerging market and developing countries as a whole.
- A review of the Fund's transparency policy is planned to start shortly after the October 2009 Annual Meetings.