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**BROOKINGS**

## ***Evaluating IMF Lending Options in Response to Global Crises***

*Roundtable Discussion*

March 6, 2012

### **Summary Findings and Conclusions**

#### **Context**

In late 2011, the International Monetary Fund (IMF) revamped its crisis lending instruments in response to members' calls for stronger global financial safety nets, particularly given the heightened financial stress in Europe and turmoil occurring in North Africa and the Middle East.

On March 6, 2012, the Bretton Woods Committee, working in cooperation with the Brookings Institution, brought senior IMF and U.S. Department of Treasury officials together with Bretton Woods Committee members and guests – including economists, academics, experts from the private sector, and former high ranking government and international financial institution officials – to evaluate these changes.

Specific lending tools discussed included the Fund's long-standing Stand-By Arrangements (SBA); the Flexible Credit Line (FCL) established in 2009; the Precautionary and Liquidity Line (PLL) established in late 2011 for member countries with strong policies, but some remaining vulnerabilities that preclude them from using the FCL; and, the Rapid Financing Instrument (RFI), also established in late 2011 to replace existing emergency assistance instruments.

#### **Revamped Crisis Lending Tools**

As the PLL and RFI have not yet been utilized by IMF members, definitive conclusions about their effectiveness were not possible. However, participants generally agreed that the Fund's revamped lending instruments appear to overcome several shortcomings of earlier tools and should better meet members' needs.

Several attendees posed questions about how the Fund defined "countries with strong policies" and whether the FCL had a clear enough call for exit strategies. Others wondered whether the terms of the new lending instruments eroded the important pricing power that the IMF can exercise as the global lender of last resort. Participants also reaffirmed the value and role of the SBA as a way to phase in structural changes and to safeguard loans.

## **Conditionality**

Participants strongly agreed on the need for the IMF to continue to incorporate strict, enforceable conditionality in its crisis lending. Several also stressed that the conditionality and expertise of the Fund were equally – if not more – important than the financial resources that it can contribute. Participants cautioned against easing conditionality under the weight of political pressures.

Several participants observed the lessons from emerging markets' experiences: the important function of a healthy banking sector in financial recovery, the role of the private sector in national lending, and how the success of IMF lending is a function of both a member's inherited conditions and a government's willingness to change. One participant noted that the new FCL helps to reduce the stigma of IMF borrowing through the high-bar set by its qualification requirements and absence of ex-post conditionality. However, it was emphasized that conditionality remains very important for IMF credibility and as a commitment device for a country's authorities.

## **Firewalls**

There was agreement that larger firewalls were needed at the international and regional levels, although there was disagreement about whether supporting regional firewalls should take precedence over strengthening the Fund's own firewall. To maintain greater legitimacy and credibility, particularly in its crisis lending to Europe, there was general agreement that the IMF should play a complementary, rather than supplemental, role to governments and regional institutions. Several participants noted the need to enforce existing conditionality for members before focusing on strengthening firewalls.

## **The IMF and Regional Relationships**

The relationship between the Fund and regional organizations, including currency unions, was a frequent topic in the discussion. Participants noted the Fund's involvement with the European Central Bank (ECB) as both a partner in the Troika and a representative of the monetary policies of its members – wondering on which side of the negotiating table the ECB belonged.

Similarly, they expressed concerns that the Fund may not be adequately managing risks; that the Fund is not adequately adapting its policy and conditionality framework with respect to members who cannot make independent changes to monetary and exchange rate policies in the context of a currency union; and, that the policy and conditionality framework may not adequately address situations where the actions of one member state create an unprecedented scope for contagion to the union as a whole. While previously some attendees appreciated a hands-off approach to the internal workings of regional bodies, there was a call for clearer and more deliberate role clarification between the IMF and these organizations.

Many participants stressed the need for the IMF to play a supplemental and complementary role to central banks and regional actors, while a handful called on member states to provide greater resources to the Fund, in order to give them greater leverage over members and regions at the negotiating table. Whether they envisaged a more systemic or a complementary financing role, several noted that the current scale of resources is not adequate.

## **Moving Forward**

In order to continue to improve the IMF's global safety nets, participants generally agreed that:

- The Fund must clarify its relationship to regional organizations, including those in currency unions, as soon as possible, with the aim of better clarifying respective accountabilities and responsibilities.
- The Fund must overcome the perceived stigma of borrowing, if it wants members to seek support in a timely and precautionary way. Enhancing national ownership of conditionality was seen as key to ensuring lasting change, building on the institution's recent efforts .
- The Fund's conditionality is as critical as its lending for developed countries, emerging markets, and developing economies alike. The Fund must continue to insist on sound policies and discipline from its members, offering support, predictability, and consistency in its approach.
- The adequacy of IMF's resources should be considered, although participants noted that any scale-up effort should be linked to similar efforts in building regional safety nets.