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INFORMAL SESSION TO ENGAGE

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June 30, 2023

To: Members of the Executive Board

From: The Secretary

Subject: **Staff Note on the 2023 Review of the Flexible Credit Line, the Short-Term Liquidity Line, and the Precautionary and Liquidity Line, and Proposals for Toolkit Reform**

Board Action:	**Informal session to engage** Executive Directors
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June 30, 2023

STAFF NOTE ON THE 2023 REVIEW OF THE FLEXIBLE CREDIT LINE, THE SHORT-TERM LIQUIDITY LINE, AND THE PRECAUTIONARY AND LIQUIDITY LINE, AND PROPOSALS FOR TOOLKIT REFORM

EXECUTIVE SUMMARY

This review of the Flexible Credit Line (FCL), the Short-term Liquidity line (SLL), and the Precautionary and Liquidity Line (PLL) comprises two elements: (i) *backward-looking*, drawing lessons from the use of the FCL, PLL, and SLL (as well as the precautionary SBA) since the 2017 review, including during the Covid-19 pandemic, and; (ii) *forward-looking*, anticipating needs of the membership to make the instruments more useful in the period ahead as external risks persist, even among countries with strong macroeconomic fundamentals.

To ensure that the toolkit remains fit for purpose at a time of heightened global risks, while safeguarding Fund resources and preserving the instruments' signaling power, the review focuses on three broad areas:

- ***Making Fund precautionary instruments available with greater flexibility and adequate firepower***, thereby making them more useful for qualifying members. Key proposals relate to accommodating extended FCL use at lower access levels (not exceeding 200 percent of quota), raising the SLL access limit (to 200 percent of quota), PLL-specific annual limit at approval (to 300 percent of quota) and PLL instrument caps (600 percent of quota cumulative), and provisions on concurrent FCL/SLL use.

- ***Refining the qualification framework*** to enhance its transparency and predictability while retaining judgment, guided by applicable criteria, core indicators and thresholds, and preserving the signaling value. Proposals include better reflection of Anti-Money Laundering/ Combating the Financing of Terrorism (AML/CFT) and governance risks in the qualification framework, and a refinement of the debt sustainability requirement for exceptional access PLLs.

- ***Ensuring the Fund's continued sound management of its precautionary instrument toolkit*** by (i) streamlining procedures related to the use of precautionary instruments; (ii) revisiting the financial aspects of Fund credit extended under precautionary arrangements—e.g., commitment fees and scoring of the forward commitment capacity (FCC), but not proposing changes in this area; and (iii) assessing the risks to the Fund of implementing this paper's key proposals, as well as risks from no action.

Options presented in the paper build in part on a survey of the membership, which calls for a coordinated outreach to better communicate the benefits of precautionary instruments, including precautionary SBAs, to country authorities.

Approved By
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Acronyms and Abbreviations

AEs	Advanced Economies
AML	Anti-Money Laundering
AMF	Arab Monetary Fund
ARA	Assessing Reserve Adequacy
BBA	Bilateral Borrowing Arrangements
BoP	Balance of Payments
BSL	Bilateral Swap Line
CFT	Combating the Financing of Terrorism
CMIM	Chiang Mai Initiative Multilateralization
CtR	Capacity to Repay
EA	Exceptional Access
EBA	External Balance Assessment
EFF	Extended Fund Facility
EMBIG	Emerging Markets Bond Index Global
EMEs	Emerging Economies
ERM	Enterprise Risk Management
ESM	European Stability Mechanism
ESI	External Stress Index
FATF	Financial Action Task Force
FCC	Forward Commitment Capacity
FCL	Flexible Credit Line
FDI	Foreign Direct Investment
FLAR	Latin American Reserve Fund
FTP	Financial Transaction Plan
GFC	Global Financial Crisis
GFSN	Global Financial Safety Net
GFSR	Global Financial Stability Report
GRA	General Resource Account
G-RAM	Global Risk Assessment Matrix
HAPA	High Access Precautionary Arrangement
HP	High Probability
IG	Investment Grade
ICC	Inflation Consultation Clause
IT	Indicative Target
MAC	Market Access Country
MPCC	Monetary Policy Consultation Clause
NAB	New Arrangements to Borrow
NIR	Net International Reserves
NPL	Non-Performing Loans
PA	Prior Action
PC	Performance Criterion

PCI	Policy Coordination Instrument
PLL	Precautionary Liquidity Line
PRGT	Poverty Reduction and Growth Trust
QPC	Quantitative Performance Criterion
RFA	Regional Financing Arrangement
SB	Structural Benchmark
SBA	Stand-By Arrangement
SCF	Stand-by Credit Facility
SDDS	Special Data Dissemination Standard
SDR	Special Drawing Right
SLL	Short-term Liquidity Line
SOE	State Owned Enterprise
SRDSF	Sovereign Risk and Debt Sustainability Framework
TBCF	Time-Based Commitment Fee
UCT	Upper Credit Tranche
WEO	World Economic Outlook
WGI	Worldwide Governance Indicators

INTRODUCTION

1. **The Fund's toolkit for precautionary financial assistance is reviewed periodically to ensure its continued relevance for crisis prevention and mitigation.** The premise is simple: preventing crises is less costly than resolving crises. The Fund's precautionary arrangements provide assurances on the availability of Fund financing in case actual balance of payments (BoP) needs were to materialize, with various instruments available to help members address different types of BoP problems while relying on ex ante qualification criteria, ex post conditionality, or a combination of the two. Qualification and/or ex post conditionality help ensure that members accessing the toolkit implement policies necessary to safeguard stability in the face of temporary, adverse external shocks.

2. **The toolkit includes four instruments in the General Resources Account (GRA).** The precautionary Stand-By Arrangement (SBA)[1] fully relies on ex post conditionality. The Flexible Credit Line (FCL) and the Short-term Liquidity Line (SLL) rely exclusively on ex ante conditionality (i.e., qualification), as well as a mid-term review for 2-year FCLs. The Precautionary and Liquidity Line (PLL) combines elements of ex ante and ex post conditionality. The previous review of the FCL and PLL, completed in 2017, enhanced the predictability and transparency of the corresponding qualification frameworks by introducing core indicators with specified thresholds for the assessment of economic fundamentals and policy frameworks.[2] The SLL, first proposed in the context of the same review, was ultimately established in early 2020 amid heightened global uncertainty and demand for liquidity at the onset of the Covid-19 pandemic.[3]

3. **Precautionary arrangements continue to be an integral part of members' toolkits.**[4] There are currently five FCLs (Chile, Colombia, Mexico, Morocco, and Peru) and two PLLs (Jamaica and North Macedonia). This represents a significant increase from two FCLs and one PLL before the pandemic. Chile became the first country to use the SLL in 2022, although it reverted to the FCL as tail risks rose.[5] Precautionary SBAs have long been a part of the Fund's lending toolkit, with six new

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[1] The precautionary Stand-by Credit Facility (SCF) serves a similar purpose under the Poverty Reduction and Growth Trust (PRGT). The SCF will be reviewed in the context of the 2024/25 PRGT review, whereas this review focuses on GRA facilities.

[2] The discussions were informed by three staff papers: "Adequacy of the Global Financial Safety Net—Considerations for Fund Toolkit Reform" (November 2016), "Adequacy of the Global Financial Safety Net—Review of the Flexible Credit Line and Precautionary and Liquidity Line, and Proposals for Toolkit Reform" (June 2017), and "Adequacy of the Global Financial Safety Net—Review of the Flexible Credit Line and Precautionary and Liquidity Line, and Proposals for Toolkit Reform—Revised Proposals" (December 2017).

[3] IMF COVID-19 Response—A New Short-Term Liquidity Line to Enhance the Adequacy of the Global Financial Safety Net (Policy Paper 20/025).

[4] The FCL and PLL are referred in this staff note as "precautionary arrangements," in line with their predominant use. However, under their respective policies, they are also available for crisis resolution. Precautionary SBAs are also included in the "precautionary arrangements" toolkit, although they are not a separate instrument from disbursing SBAs. Finally, it is the authorities' choice whether to treat the arrangement as precautionary or with the intention to make drawings in the event of actual BoP needs and subject to the terms of the arrangement.

[5] See Annex 1 for a list of FCLs, PLLs, and precautionary SBAs approved by the Fund since the last review.

precautionary SBAs approved since 2017 (Armenia in 2019, Honduras in 2019, Armenia, Georgia, and Serbia in 2022, and Kosovo in 2023).[6] Analytical work shows that members with existing and new FCL arrangements enjoyed better financing conditions than peers, helping reduce acute external financial pressures faced by emerging market economies (EMEs) in the Spring of 2020.[7]

4. The current review of the FCL, PLL, and SLL has two overarching goals. First, *looking backward*, it draws lessons from the use of the FCL, PLL, and SLL (as well as the precautionary SBA) since the 2017 review, including during the Covid-19 pandemic. Second, *looking forward*, it assesses how these instruments can be made more useful in the period ahead as external risks persist, even among countries with strong macroeconomic fundamentals.

5. This review comes at a time of heightened global challenges and aims to ensure that precautionary instruments remain nimble enough to address potentially increased demand. The global growth outlook is the weakest in decades (WEO, Spring 2023). Major central banks have notably tightened monetary policy to combat inflation, and fiscal space across many countries is constrained following the unprecedented support provided during the Covid-19 pandemic. Downside risks are also elevated, including from possible fragmentation of the global economy (and potentially to the global financial safety net itself) that give rise to potential BoP needs and may further increase demand for—and benefits from—precautionary arrangements.

6. Given elevated global vulnerabilities, the review will focus on making the toolkit fit for purpose, while safeguarding Fund resources and preserving the instruments' signaling power. The review will ensure that a clear, transparent, and appropriately strong qualification framework remains in place, and that any instrument design changes preserve their strong signaling value. This means that the possible greater use of these instruments going forward would be driven by stronger interest from qualifying members without compromising the qualification standards—in effect, *lowering the barriers without lowering the bar*.

7. To this end, the review follows a three-pronged approach:

- ***Making Fund precautionary instruments available with greater flexibility and adequate firepower to respond to potentially higher demand in the period ahead***, and making such instruments more useful for qualifying members. Key proposals relate to accommodating extended FCL use at lower access levels (not exceeding 200 percent of quota), raising the SLL access limit (to 200 percent of quota) and PLL-specific annual limit at approval (to 300 percent of quota) and PLL instrument caps (600 percent of quota cumulative), and introducing explicit provisions on concurrent FCL/SLL use. Options to facilitate synchronized take-up of the SLL by multiple countries and to develop an outreach plan to increase awareness about precautionary arrangements are also discussed.

[6] Serbia intends to treat the SBA as precautionary during the second year of the program.

[7] Lisi, Giulio, 2022, "IMF's Precautionary Lending Instruments: Have they Worked?" IMF Working Paper WP/22/256. Box 3 below provides a summary.

- ***Refining the qualification framework*** to enhance its transparency and predictability while retaining judgment guided by applicable criteria, core indicators and thresholds, and preserving the signaling value.

- ***Ensuring the Fund's continued sound management of its precautionary instrument toolkit*** by (i) streamlining procedures related to the use of precautionary instruments; (ii) revisiting the financial aspects of Fund credit extended under precautionary arrangements—commitment fees and scoring of the forward commitment capacity (FCC)—but not proposing changes in this area; and (iii) assessing the risks to the Fund of implementing this paper's key proposals, as well as risks from inaction.

Box 1. Proposals to be Discussed with Executive Directors for the Informal Session to Engage

Increase accessibility and firepower of instruments in an environment of heightened risks:

- **Exit –** State- rather than time-dependent exit, FCLs of access not exceeding 200 percent of quota free of exit expectations (consistent with residual risks).
- **Cumulative access limits –** Increase permanently the cumulative cap for access under the PLL to 600 percent of quota and the access limit under the SLL to 200 percent of quota.
- **SLL-FCL concurrent use** – Explicitly permit concurrent use of the FCL and SLL.
- **Synchronized SLLs** – Outline procedures to facilitate synchronized take-up of the SLL by multiple countries.
- **Outreach –** Develop an outreach plan to increase awareness about precautionary arrangements, including the precautionary SBA.

Reinforce that qualification is a judgment-based process informed by criteria, core indicators, and thresholds, and clarify requirements:

- **AML/CFT** – Explicitly integrated in the qualification assessment as part of the effective financial sector supervision criterion.
- **Governance** – The assessment of institutional strength in the qualification framework aligned with the 2018 Governance Framework, relying on the Fund's internal and holistic assessment of corruption vulnerabilities and governance weaknesses linked to corruption. Staff's assessment of government effectiveness and control of corruption, including in related Article IV Consultation staff report discussion where applicable, will indicate the governance and corruption vulnerabilities of a member.
- **Political assurances in the face of upcoming elections** – Reiterate requirement and consider shorter arrangements to delink approvals from the election cycle where feasible.
- **FCL safeguards policy** – Align with the safeguards policy requirement for a framework between central banks and finance ministries for servicing Fund obligations when purchases are drawn for budget financing.
- **Debt sustainability requirements** – No tightening, with a refinement: no requirement for "sustainable with high probability" assessment in drawing scenario for Exceptional Access (EA) PLLs, but debt on a decreasing path or at least stabilizing debt ratio over five years.

Streamline procedures to make arrangements more easily usable and more flexible:

- **Number of Board meetings** – For approvals of new arrangements (back-to-back Article IV/Informal for FCLs/PLLs), renewals (no informal for successor FCLs/PLLs) and reviews (combined with Article IV for FCLs/PLLs, with clear and transparent separation of the FCL/PLL related sections and Surveillance discussions in the relevant reports, should the team consider the option of a single staff report).
- **SLL requirements** – Adverse scenario not required to justify SLL access, option of requesting an SLL, simpler transition between FCLs and SLLs (see below).
- **Streamlined FCL augmentation process and synchronized FCL requests to augmentations** – Staff reports can cross-reference qualification analysis in previous Board documents if the latter is less than 6 months old. Synchronized FCL augmentations are proposed (similar to synchronized FCL approvals).
- **Transition from SLL to FCL (or vice versa), and transition from stand-alone SLL or FCL to concurrent use of FCL and SLL** – Staff reports can be streamlined as per above and informal Board dropped for transition from SLL to FCL if previous arrangement has been approved/reviewed less than six months ago.

USE AND BENEFITS OF PRECAUTIONARY INSTRUMENTS

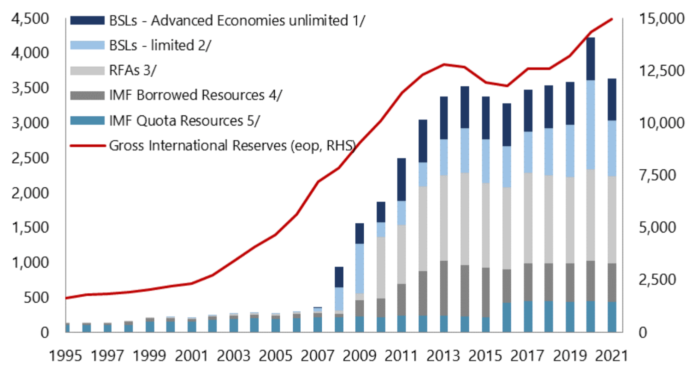
This section summarizes the analytical evidence on the use and benefits of precautionary arrangements, while situating the demand for precautionary arrangements in a broader context of the global financial safety net (GFSN) and its various layers.

A. Precautionary Arrangements Within the Global Financial Safety Net

8. The GFSN has grown substantially over the last 15 years. Perks et al. (2021) estimate it at around US$18.6 trillion at end-2021, compared to US$12 trillion as of end-2010, with bilateral swap lines (BSLs) and regional financing arrangements (RFAs) becoming a larger part of it in the early 2010s (Figure 1).[8] In particular, BSLs started to expand during the global financial crisis (GFC), as the Fed extended BSLs to five major central banks in advanced economies (AEs), as well as to central banks of other AEs and large EMEs to ease pressure in dollar funding markets.[9] During this period, China also expanded its BSL network to promote internationalization of the renminbi and to facilitate trade and investment.

Figure 1. Evolution of the GFSN, 1995 – 2021

(billions of U.S. dollars)



Notes: Two-way arrangements are counted only once.
1/ Permanent swap lines among major advanced economy central banks (Fed, ECB, Bank of England, Bank of Japan, Swiss National Bank, Bank of Canada). The estimated amount is based on known past usage or, if undrawn, on average past maximum drawings of the remaining central bank members in the network, following the methodology in Denbee et al. (2016, Bank of England Financial Stability Paper).
2/ Limited-amount swap lines include all arrangements with an explicit amount limit and exclude all CMIM arrangements, which are included under RFAs.
3/ Based on explicit lending capacity/limit where available, committed resources, or estimated lending capacity based on country access limits and paid-in capital.
4/ After prudential balances.
5/ Quota for countries in the Financial Transaction Plan (FTP) after deducting prudential balance.

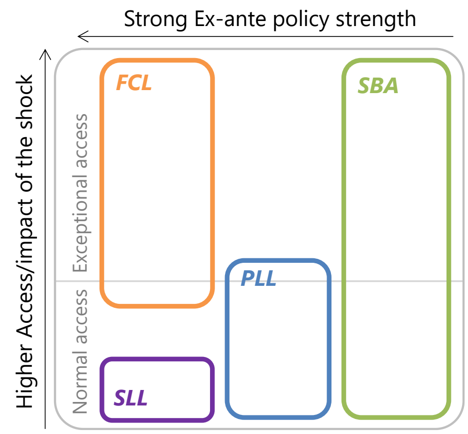
Sources: Central Bank websites; RFA annual reports; and IMF staff estimates.

[8] Perks et al., 2021, "Evolution of Bilateral Swap Lines," IMF Working Paper WP/21/210, estimate gross international reserves at US$15 trillion, BSLs at US$1.4 trillion, RFAs at US$1.2 trillion, and the IMF at US$1 trillion.

[9] The BSLs with the five major central banks were renewed in 2010 and converted into permanent standing facilities in 2013, while BSLs with other AE and EME central banks were allowed to expire as market conditions improved. The Fed also announced extensions of its FIMA repo facility, which is distinct from BSLs (see Perks et al, 2021, for details). Bilateral swap lines also expanded during the Covid-19 pandemic (in 2020, see chart).

9. An important component of the GFSN, the Fund's lending toolkit includes several precautionary instruments (Figure 2, or Annex II for details). The choice of an appropriate instrument depends on the nature of a country's BoP needs, its economic fundamentals, policy frameworks, and track record. While all Fund members are *eligible* to use the FCL/SLL and the PLL, only countries with very strong and sound economic fundamentals and institutional policy frameworks, respectively, would meet the *qualification criteria* to use these instruments. In contrast, the SBA does not have similar ex ante qualification criteria and is available to the entire membership, including as a precautionary instrument if needed.[10] The FCL, PLL, and SBA can be approved when countries face actual, prospective, or potential BoP needs, while the SLL can only be approved for countries with potential BoP needs at approval. The FCL and SBA have no cap on access, while the PLL currently has a cumulative access cap of 500 percent of quota, applicable to all PLL arrangements, regardless of duration.[11] Access under the SBA and PLL is also subject to the Exceptional Access (EA) policy, while access under the SLL, which was designed to cover only potential moderate short-term BoP needs, is capped at 145 percent of quota.[12] This review focuses on precautionary arrangements with ex ante qualification—the FCL, SLL, and PLL—while highlighting the continued relevance of the precautionary SBA, including High Access Precautionary Arrangements (HAPAs). It is worth noting though that the precautionary instruments that do embed ex post conditionality (the precautionary SBA and the PLL) can help support the country's policy mix and reform agenda.

Figure 2. De Facto Use of the IMF Precautionary Toolkit



Note: The line refers to the normal cumulative access limit under the GRA (435 percent of quota).

10. The demand for precautionary arrangements in recent years was likely influenced by the availability of other layers of the GFSN. The 2021 SDR allocation, BSLs, and RFAs provided a significant top-up to existing reserves for many EMEs. On the whole, while GFSN buffers have

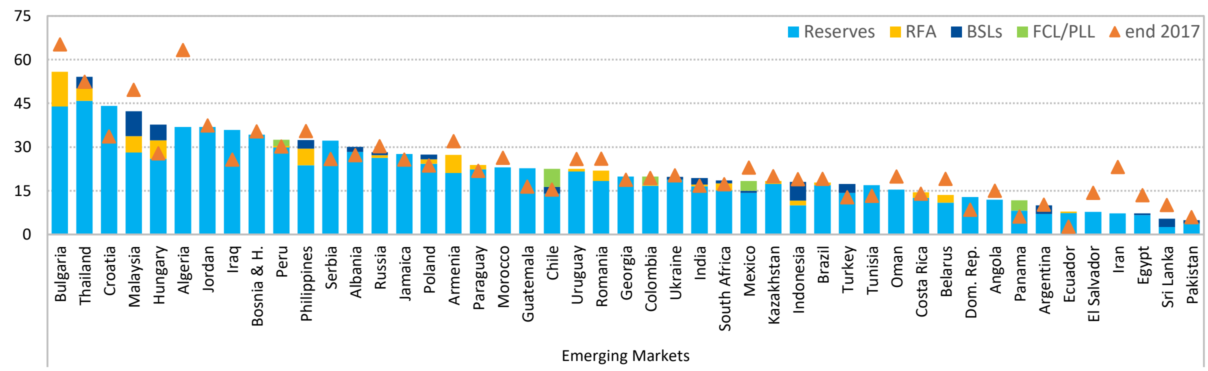
[10] Additionally, the Stand-By Credit Facility (SCF), available to PRGT-eligible members, can also be extended on a precautionary basis. The SCF is not discussed in this paper separately, since it will be taken up in the next review of concessional instruments; however, the discussion of the precautionary SBA largely applies to the SCF as well.

[11] The current 500 percent of quota cumulative cap under the PLL instrument was above the cumulative access limit in the GRA until the recent temporary increase of this limit to 600 percent of quota. In addition to the 500 percent of quota cumulative access cap under the PLL instrument, access to Fund resources through six-month PLL arrangements (i) cannot exceed a cumulative 6-month PLL arrangement access cap of 250 percent of quota, and (ii) are subject to a per arrangement limit of 125 percent of quota (or 250 percent of quota, in exceptional circumstances where a member is experiencing or has the potential to experience larger short-term BoP needs owing to the impact of exogenous shocks, including heightened regional or global stress conditions).

[12] It is also worth noting that FCL, PLL, and SBA are instruments in the GRA credit tranches and share the same lending terms (fees, charges, repurchase period, etc.). The SLL has different features (lower fees, shorter repayment period, and revolving financing), having been created as a special facility outside of the credit tranches to help address a special BoP problem.

declined since the last review for some countries, they exceed 20 percent of GDP for many EMEs (Figure 3). As such, they have provided a substantial financing alternative to the Fund's precautionary arrangements, especially since 2020. This finds support in the survey of country authorities undertaken as part of the review (see Annex VII for details), where respondents note the availability of BSLs, RFAs, and other sources of financing (such as donor support) having a bearing on their take-up of PLLs and precautionary SBAs. The lower availability of other layers of the GFSN compared to other regions could have also contributed to the concentration of FCLs in the Western Hemisphere (Box 2). Going forward, demand for precautionary arrangements could increase as global liquidity becomes less easily available. Besides, the introduction of the RSF, which can only be requested under a concurrent IMF-supported UCT program (for example, SBA, PLL, or FCL), could at the margin also increase future demand for precautionary arrangements. Surveyed members did not cite perceived stigma from associating with the Fund as the main factor influencing the demand for precautionary arrangements. However, the respondents' sample may not necessarily be representative of the whole membership, as it overrepresents members from some regions and current and past users of precautionary arrangements.[13]

Figure 3. GFSN Buffers of Select EMEs at end-2022, in Percent of GDP



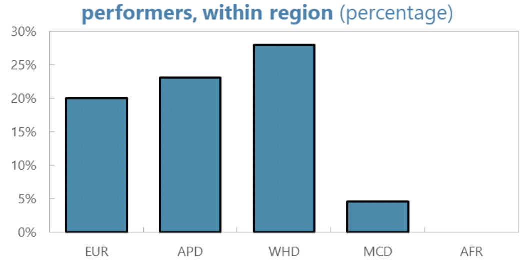
Sources: World Economic Outlook, Central Bank websites, RFA annual reports, and IMF staff calculations and estimates.

[13] See Box 3 of the IMF policy paper "Adequacy of the Global Financial Safety Net—Considerations for Fund Toolkit Reform" (November 2016) for details on the sources of stigma associated with Fund arrangements.

Box 2. Regional Concentration of FCL and PLL Arrangements

As of end-2022, most FCL and PLL arrangements were concentrated in the Western Hemisphere, representing around 50 percent of total credit committed under the GRA, or 93 percent of total credit committed under precautionary arrangements (including SBAs). Commitments under the five ongoing FCLs amount to almost SDR 65 billion, while the Jamaica and North Macedonia PLL arrangements represent commitments of SDR 1.1 billion, out of SDR 129 billion committed under current GRA arrangements.

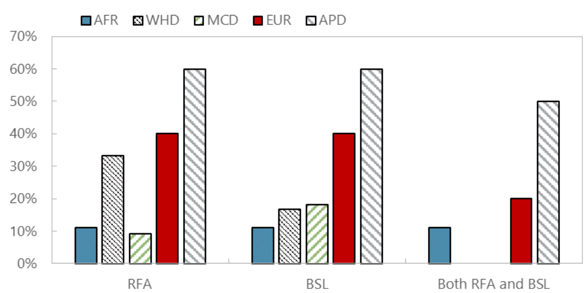
Share of EMEs considered strong performers, within region (percentage)



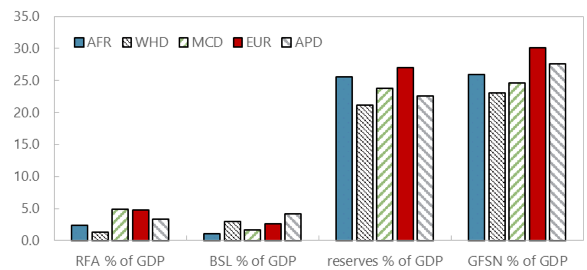
Reading note: 20 percent of EUR countries are considered strong performers, as per the criteria outlined in the text.

A possible reason for such concentration may be the share of countries potentially qualifying for FCL and PLL arrangements within each region. To roughly proxy the qualification requirements, staff calculated the share of EMEs within each region that have: (i) a public debt ratio below 70 percent of GDP; (ii) international reserves above 80 percent of the ARA metric; (iii) single-digit inflation; and (iv) external gross financing needs lower than 15 percent of GDP. This simple exercise points to the prevalence of countries in the Western Hemisphere, Asia Pacific, and Europe regions among potential qualifiers.

Share of countries having a RFA or BSL, by region (percent)



GFSN buffers
(as a share of GDP, for countries for which the GFSN layer is available)



Sources: World Economic Outlook, Central Bank websites, RFA annual reports, and IMF staff calculations and estimates.

Additionally, Western Hemisphere EMEs generally have a lower availability of alternative sources of financing, in particular international reserves and RFAs, than Asian and European EMEs. EMEs in the Western Hemisphere have somewhat lower reserve coverage. A relatively large share of EMEs in the Western Hemisphere has either an RFA or a BSL, but the FLAR—the Western Hemisphere RFA—is smaller (at 1.3 percent of GDP on average for member countries) than RFAs in other regions (4.1 percent of GDP on average). All in all, the lower size of GFSN buffers for EMEs in the Western Hemisphere (23 percent of GDP on average), compared to EMEs in other regions (27 percent of GDP on average), could explain the concentration of precautionary arrangements in that region. This was highlighted as a reason by the authorities in the survey too (Annex VII).

Ultimately, regional concentration may not be a concern. First, while take up could be considered low in some regions, not all the countries with very strong (or sound) fundamentals potentially qualifying for precautionary instruments are expected to make use of those, especially at times of relatively abundant global liquidity. Second, with the Fund being at the core of the GFSN, a less diversified portfolio—compared to other financial institutions—is justified, including because economic shocks, contagion, and risks often have a regional element. Third, the regional concentration of Fund lending (such as in Asia and Europe in recent decades) has evolved over time. Finally, in the context of FCLs and PLLs, the high qualification standards provide safeguards to Fund resources and limit the risks from regional concentration.

B. Precautionary Arrangements vs. Other Layers of the GFSN

11. Precautionary arrangements have contributed to market confidence, acting as insurance for member countries. Analytical work summarized in Box 3 shows that the announcement of a new FCL or PLL arrangement generally leads to a significant decline in sovereign spreads, especially for FCLs. Precautionary arrangements—which allow for an immediate drawdown in case a BoP need materializes—have helped countries cushion external shocks during the pandemic, with FCL and PLL drawdowns having had no adverse market impact. Authorities have also highlighted the additional policy space afforded by precautionary arrangements, which allowed them to pursue countercyclical policy in response to the pandemic. In general, precautionary arrangements carrying ex ante conditionality also incentivize very strong (or sound) policies.

12. The costs and terms of FCL and PLL arrangements are favorable compared with market rates, particularly during episodes of market stress. FCL and PLL arrangements, which are subject to the same charges and surcharges as other GRA facilities, can be more cost effective than market financing when drawn, particularly in times of market turbulence. The basic rate of charge is equal to the SDR interest rate, which is a weighted average of short-term interest rates for the SDR basket currencies, plus a moderate fixed margin.[14] Apart from the basic rate of charge, drawing FCL and PLL arrangements are also subject to commitment fees, a service charge, as well as level- and time-based surcharges.[15]

[14] See also Figure 8 in "Review of The Adequacy of The Fund's Precautionary Balances", December 2022.

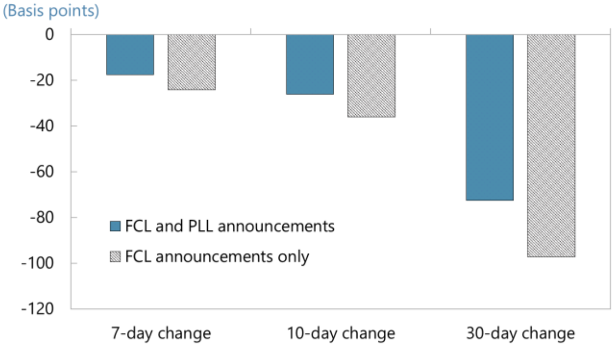
[15] The service charge is 50 bps upon drawing. A two-percent surcharge applies to the portion of outstanding borrowings exceeding 187.5 percent of a member's quota, and an additional one percentage point applies to this portion if these balances have been outstanding for more than 36 months (more than 51 months in case of borrowing under the Extended Arrangement (EFF)).

Box 3. Precautionary Lending Instruments and Market Confidence

Previous reviews have highlighted favorable effects of the FCL and PLL on market sentiment and outcomes. Event studies in the 2011 Review of the FCL and PCL found a decline in sovereign spreads following the announcement of a new FCL arrangement. Cross-sectional regressions in the 2014 Review of the FCL, PLL, and RFI showed that the announcement of a new precautionary arrangement resulted in higher capital inflows and lower spreads. The 2014 Review also found that countries with a PLL or FCL experienced a more limited increase in spreads compared to other EMEs following the Fed tapering announcement in 2013. The 2017 Review of the FCL and PLL used event analyses to show muted market reactions to reductions in access.

Empirical analysis conducted for the current review shows that the announcement of a new FCL or PLL arrangement leads to a decline in sovereign spreads.[1/] This exercise uses event study difference-in-difference regressions to identify movements in sovereign spreads resulting from the announcement of a new FCL or PLL arrangement. Using a sample of FCL and PLL arrangements approved through January 2021[2/] and controlling for global risk factors such as the VIX index, oil prices, U.S. bond term spreads, and country fixed effects, the analysis finds evidence of a large drop in spreads for FCL and PLL users, ranging from 17 to 24 basis points in the seven trading days following the announcements, rising to over 70 basis points on average in the following 30 trading days). The effect for FCLs is stronger. Additional country-level analysis using the synthetic control method broadly corroborates the positive and persistent effect of these arrangements on market confidence, in particular for FCLs.[3/]

Average Change in EMBI Spreads around FCL and PLL Announcement Dates
(Basis points)



Sources: G. Lisi (2022) IMF's Precautionary Lending Instruments: Have They Worked?

The analysis also finds that FCL and PLL arrangements helped mitigate external financial pressures during the COVID-19 pandemic. Using panel regressions over 2019Q2-2020Q3, the study compares variations in spreads at the onset of the pandemic across precautionary arrangement adopters and non-adopters.[4/] Econometric results show that countries with an FCL or PLL arrangement in place during the pandemic experienced lower increases in spreads relative to other EMEs, after controlling for country-specific effects, time effects, and global and domestic drivers of sovereign spreads.[5/] Specifically, sovereign spreads were approximately 7 percent lower in countries with an FCL or PLL arrangement relative to other EMEs, confirming the important role of precautionary arrangements in cushioning external financing pressures.

Box 3. Precautionary Lending Instruments and Market Confidence (concluded)

Finally, the analysis shows that FCL and PLL drawdowns have had a limited impact on market sentiment. The analysis examines the only two instances, in 2020, where countries drew on resources available under their precautionary arrangements—Colombia's partial purchase under the FCL and Morocco's full drawdown of the PLL. Simulation-based event studies reveal that, while average sovereign spreads declined by 7.2 basis points in Colombia and 9.3 basis points in Morocco in the 30 trading days following drawdowns, these variations were not statistically significant, suggesting no evidence of an adverse effect on market confidence.

1/ Lisi, 2022.

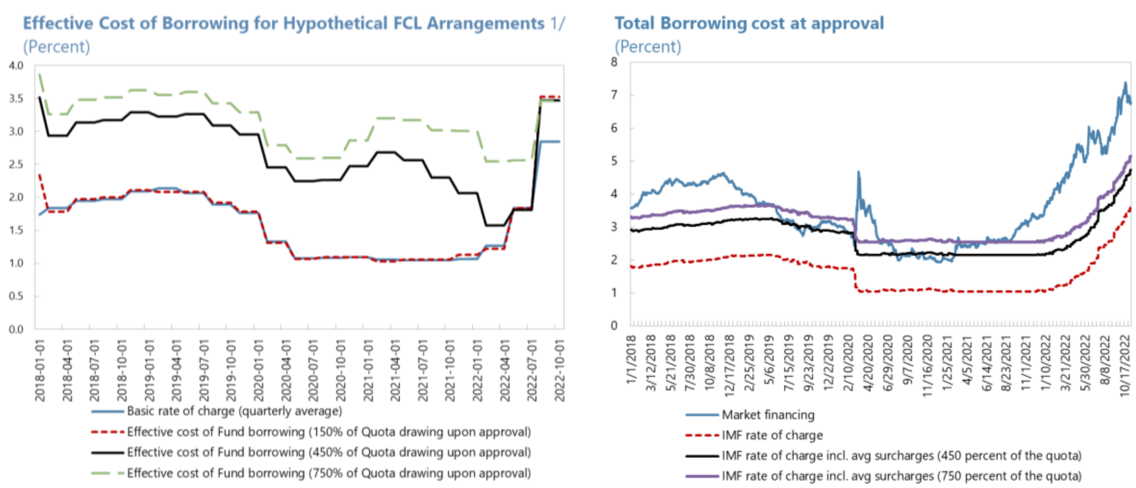
2/ The sample includes (i) FCL arrangements for Colombia, Mexico, Poland (all announced in 2009), Chile and Peru (both announced in 2020); and (ii) PLL arrangements for Morocco and Panama announced in 2012 and 2021, respectively.

3/ Panama's PLL was announced when market pressures resulting from the COVID-19 pandemic had already largely subsided, potentially explaining the muted market reactions. For other countries in the sample, the timing of the announcement of a new FCL or PLL generally coincided with periods of relatively high sovereign spreads, consistent with precautionary arrangements' objective of helping members to withstand external shocks amid stressed market conditions (IMF, 2011).

4/ During this period, Chile, Colombia, Mexico, and Peru had an FCL in place, while Morocco had a PLL.

5/ Domestic drivers of spreads include the fiscal balance, external current account balance, foreign reserves, public debt, and a political risk index.

Figure 4. FCL Repayment Profile and Borrowing Costs



Source: IMF staff estimates.

1/ The scenarios assume that the hypothetical FCL arrangement was drawn in full at approval on January 1, 2018. Effective costs are calculated by dividing the payment of charges and surcharges by the average amount of credit outstanding in each financial quarter and then annualizing the rate.

Note that at the end of the period, surcharge payments do not apply even under higher-access (450 and 750 percent) scenarios but the decline in credit outstanding (denominator) is more pronounced under the lower-access (150 percent) scenario. As a result, the effective cost under the lower-access scenario is marginally higher compared with the higher-access scenarios at the end.

- Figure 4 (left-hand side chart) illustrates the cost of borrowing for hypothetical FCL arrangements of different access levels, assuming the member would draw in full upon approval in January 2018.[16] Owing to surcharges applied to the portion of the GRA credit outstanding exceeding 187.5 percent of quota, an FCL arrangement of 450 or 750 percent of quota has an effective cost that is, on average, about 1 or 1½ percentage points larger than the effective cost of an FCL arrangement of 150 percent of quota (which de facto equals the basic rate of charge apart from the service fee), respectively.

- Figure 4 (right hand side chart) compares the net present value of costs of FCL arrangements *at approval* (proxied by the weighted average of the basic rate of charge for the portion of credit below the threshold of 187.5 percent of quota, and the basic rate of charge plus surcharges for the portion of credit above that threshold) with market financing costs for qualifying members, proxied by the 5-year U.S. T-bond rate plus the average EMBI spreads of current FCL users. Over the last five years, the basic rate of charge of IMF instruments was on average 2 percentage points lower than market financing. This difference rose in recent episodes of market distress—the onset of the pandemic and the tightening of global financing conditions at end-2022—to about 4 percentage points—showing that FCLs and PLLs fulfill the role of insurance well. Owing to surcharges, the average cost advantage of an FCL arrangement of 450 or 750 percent of the quota vis-à-vis market financing was smaller—about 1 and ½ percentage points over the last five years, respectively.

13. Precautionary arrangements can be cheaper than holding reserves when used on a precautionary basis. For current FCL users, the cost of holding reserves[17] constituted around 220 bps during 2018–22, compared to a 26 basis-point effective commitment fee for an illustrative IMF precautionary arrangement of 450 percent of the quota, translating into a saving of about 0.12 percent of GDP per year. Lisi (2022) also shows that government borrowing costs can decline up to 70 basis points after the announcement of an FCL approval (Box 3). Given the average government debt level of current FCL users (about 50 percent of GDP), this could imply savings of about 0.33 percent of GDP per year, suggesting that FCL arrangements on a precautionary basis could have led to almost ½ percent of GDP in savings during 2018–22 relative to increasing reserve holdings.

14. However, some aspects of precautionary arrangements could make them less desirable to countries than the BSLs. Precautionary arrangements, as opposed to BSLs, have the advantage of being provided by a multilateral institution, with clear and transparent qualification rules, and immediate availability of financing when a shock hits. While information on BSLs and RFAs is limited

[16] PLL and FCL costs are identical. We assume here an FCL arrangement owing to the PLL access cap at 500 percent of the quota.

[17] The cost of holding reserves is being calculated as the cost of building reserves, proxied by a 5-year borrowing cost (5-year US T-bond rate plus EMBI spread) minus the return on reserves (estimated as the average of the 3-month and 2-year US T-bill rate).

and often not publicly available, Perks et al. (2021) shed some light though on some terms and conditions of BSLs that could make them more attractive than the Fund's precautionary arrangements. First, apart from the Fed's BSLs with the five major central banks, which have been established on a standing basis since 2013, many other BSLs have a duration of three years, which is longer than the usual duration of precautionary arrangements—PLLs and FCLs have a maximum duration of two years—although precautionary arrangements can also be renewed. BSLs also provide revolving access, a feature shared only by the SLL. Second, BSLs are more likely to be signed when a country's external position is weakening, which might make them more accessible compared to precautionary arrangements that are granted only to countries whose fundamentals are very strong or sound (and therefore should not have deteriorated significantly). Finally, BSLs have no associated ex post conditionality and may therefore be perceived to carry less stigma than the PLL or precautionary SBA. On the other hand, it is worth mentioning that the extension or continuation of a BSL is usually at the discretion of the reserve currency issuer, which increases uncertainty and reliance on a bilateral relationship, in contrast with the Fund's precautionary arrangements offered by a multilateral institution and based on clearly defined and transparent qualification. Finally, the use of BSLs on a large scale remains untested, including during periods of stress, which provides further support for the Fund to play a key role to provide this type of insurances.

15. While most RFAs have precautionary and liquidity support tools, their preventive stabilization role remains largely untested (Box 4). Lending by smaller RFAs (AMF and FLAR) has been mostly concentrated on assisting fragile economies in the region, while the precautionary tools offered by the largest RFAs (ESM and CMIM) have not been deployed so far and their stabilization effect can thus not be assessed with certainty.[18] The regional approaches to preventive stabilization continue to be developed.

16. Precautionary arrangements with ex post conditionality have continued to prove helpful in recent years and offer notable flexibility. While not all members qualify for an FCL, SLL, or PLL, most members can take advantage of the Fund's precautionary SBAs. PRGT-eligible members are also eligible for precautionary SCFs. Five countries have used precautionary SBAs since the last review. The case studies (Annex IV) highlight their flexibility. Access under precautionary SBAs is uncapped and can be augmented quickly: Armenia augmented its 2019 precautionary SBA and drew on it during the pandemic. Additionally, SBAs allow for hybrid use: starting as a disbursing arrangement and turning precautionary a couple of reviews into the arrangement, as done by Serbia 2022. Besides, they can send a strong policy commitment signal, even at low access, as was the case in Armenia's 2022 precautionary SBA of 100 percent of quota. Policy Coordination Instrument (PCI) users can also switch to a precautionary SBA if potential BoP needs for Fund resources materialize (Serbia), while concurrent use of the PCI with the SBA/SCF is also feasible (Senegal, 2021), and a precautionary SBA can be the basis for an RSF request too (Kosovo, 2023). Since 2017, one country, Honduras, also took advantage of the precautionary SCF, through a blended SCF/SBA, after having

[18] See footnote 25 for the RFAs' full names. There is some evidence on the announcement effects of the ESM's Pandemic Crisis Support. See Anev and Ruhl, 2020, "Why the Covid-19 credit line still makes sense", available at https://www.esm.europa.eu/blog/why-covid-19-credit-line-still-makes-sense.

had two other similar arrangements in 2010 and 2014 and drew on it after an augmentation during the pandemic.

Box 4. Precautionary and Liquidity Support by RFAs[1/]

While most RFAs have precautionary and liquidity support instruments in their lending toolkits, the degree of their operationalization varies.[2/] Smaller RFAs (AMF, FLAR) that are active lenders concentrate on supporting fragile economies in the region, with their preventive stabilization capacity for stronger members constrained by their limited lending capacity.[3/]

Some RFA instruments that are intended for short-term liquidity support provide limited access to funding with no conditionality. The AMF's Automatic Loan and its Short-Term Liquidity Facility have no instrument-specific conditionality or qualification criteria; however, Automatic Loans can be used in conjunction with other AMF instruments that require conditionality. The FLAR also offers short-term liquidity support, though higher access is subject to an availability commission and requires a debtor's guarantee.

The RFAs with the largest lending capacity (ESM and CMIM) have actively engaged in developing their precautionary support tools, but their preventive role remains untested:

- **CMIM.** Qualification criteria for the CMIM's Precautionary Line cover the same areas as the FCL/SLL/PLL and the CMIM has taken steps to further align with IMF practice. The legal framework governing its conditionality has been strengthened, embedding a requirement for consistency with the IMF in co-financing situations. At the same time, the threshold for the access amount that does not require engagement with the IMF (IMF de-linked portion) has been increased to 40 percent of a maximum arrangement amount. The CMIM has also clarified the review requirements, increased flexibility for the instrument's renewal, and adjusted the disbursement terms, though the six-month repayment remains significantly shorter compared to repayment under the IMF facilities.

- **ESM.** The recent 2020 ESM toolkit reform also aimed at enhancing the efficiency of precautionary assistance and predictability of ex ante qualification, concluding with an agreement that revised the eligibility requirements and revamped credit line governance, including functioning of the periodic reviews. The ESM reform will become effective upon ratification of an amended ESM Treaty. The ESM's Pandemic Crisis Support was also based on the ESM's credit line framework, with temporary modifications in the financing terms and conditionality.

The 2017 RFA paper established that effective firepower of the GFSN and its timely deployment could be increased through enhanced IMF-RFAs cooperation.[4/] The lending-related priorities that were identified in the 2017 paper remain relevant, notably the need to ensure a consistent macroeconomic framework in IMF-RFA co-lending and alignment of qualification standards when delivering precautionary assistance. The IMF may also provide support to RFAs in their efforts to develop regional approaches to preventive stabilization.

1/ Prepared by Rimtautas Bartkus (SPR).
2/ The RFAs considered in this box include the Arab Monetary Fund (AMF), the BRICS Contingent Reserve Arrangement (CRA), the Chiang Mai Initiative Multilateralization (CMIM), the Eurasian Fund for Stabilization and Development (EFSD), the European Stability Mechanism (ESM), and the Latin American Reserve Fund (FLAR). The EFSD does not have a dedicated instrument for precautionary or short-term liquidity support in its toolkit, whereas the information available on the CRA modalities is limited.
3/ For example, access under the 2020 FCL for Colombia was over two times the FLAR's total lending capacity ($7.9 billion in 2021). Additionally, Morocco purchased SDR 2.15 billion under the PLL in 2020, compared to SDR 247 million provided under the AMF facilities in the same year.
4/ IMF, 2017, "Collaboration between Regional Financing Arrangements and the IMF."

QUALIFICATION FRAMEWORK

This section reviews the experience with the FCL, SLL, and PLL by assessing the application of the qualification framework. Additionally, it presents proposals to better account for governance and Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) risks and proposes a refinement to the debt sustainability requirement for exceptional access precautionary PLLs without compromising safeguards.

A. Core qualification Indicators and Thresholds

FCL and PLL qualification assessments undertaken since the last review have been transparent and in line with instruments' corresponding Guidance Notes, based on *judgment, guided by relevant qualification criteria, core indicators, and thresholds*.

17. The introduction in the 2017 review of a set of core indicators to anchor the qualification assessment has facilitated more predictable and transparent qualification assessments. These indicators, with their associated thresholds, have helped ensure greater comparability across qualification assessments (see Annex and Figure 5): [19]

- FCL countries have generally performed "very strongly" against core indicators. EBA bottom-line assessments are roughly equally distributed between "broadly consistent," "moderately weaker than," and "moderately stronger than" the level implied by fundamentals and desirable policies.
- The median private capital flows share over total capital flows was 76 percent, generally well above the required 50 percent threshold.
- The median reserve coverage was 139 percent of the ARA metric, also well above the 100 percent threshold.
- Almost all FCL countries issued an international bond in each of the five years preceding the qualification in the average cumulative amount of several hundred percent of quota, well above the required 50 percent.
- Debt was assessed in all cases to be sustainable with a high probability under the baseline. All FCL countries have sovereign bonds with investment grade (IG) rating except Colombia and Morocco, which are rated one notch below IG.

[19] See FCL Operational Guidance Note, August 2018, paragraph 5, for a more comprehensive reference to the qualification criteria and core indicators.

- Above all, FCL countries have well-established fiscal frameworks, guided by transparent fiscal rules and medium-term fiscal strategies, as well as a credible inflation targeting framework (or have been moving towards it).[20]

- Exchange rate flexibility also acts as a key shock absorber in most FCL countries.[21]

- Inflation in FCL countries has averaged 4.3 percent in the three years preceding the request.

- The financial system of FCL countries has been sound, with the banking sector capital adequacy ratio averaging 16.4 percent and NPL ratios of around 3.8 percent over 2019-22.

- Finally, FCL countries were assessed to have effective financial supervision and are all Special Data Dissemination Standard (SDDS) subscribers or Special Data Dissemination Standard Plus (SDDS Plus) adherents.[22]

18. PLL qualifiers were also found to perform adequately against core indicators. In particular:[23]

- The EBA assessments of the four PLL qualifiers during 2018-22 were "broadly consistent" or "moderately stronger" than the level implied by fundamentals and desirable policies.

- The share of private flows in total capital flows was similar to that of FCL users, at around 75 percent.

- While Panama, Jamaica, and North Macedonia had issued several international bonds during at least three of the five years preceding qualification in an average cumulative amount of over 1,106 percent of the quota, Morocco—which had a PLL from 2012 to 2020, before transitioning to an FCL in 2023—had not issued in international markets (but maintained a relatively favorable rating). Panama is the only PLL country whose government bond was rated as investment grade.

- For most PLLs, reserves of PLL countries were lower than that of FCL countries, slightly higher than 100 percent of the ARA metric.

[20] Over the last few years, Morocco has made significant progress in their planned transition to an inflation-targeting regime with IMF technical support and is expected to move forward with the final stages of the transition once inflation and uncertainty on global and domestic outlook are lower.

[21] Morocco is the only FCL user with a pegged exchange rate within horizontal bands, as per AREAER.

[22] The core indicator on data transparency and integrity requires that the member is a Special Data Dissemination Standard (SDDS) subscriber or has made satisfactory progress toward meeting the SDDS requirements.

[23] See PLL Operational Guidance Note.

- Debt was assessed in all cases to be sustainable with a high probability under the baseline, and under the adverse scenario in EA cases. Panama and Jamaica had fiscal rules and a medium-term fiscal framework, while the fiscal framework in North Macedonia is still developing.[24]

- While Jamaica has a floating exchange rate regime, Morocco has a peg, North Macedonia a de-facto peg, and Panama a fully dollarized economy. Inflation in PLL countries was slightly lower than in FCL countries, at about 3.5 percent on average in the three years preceding PLL requests.

- The financial system of PLL countries is sound, with the banking sector capital ratio averaging 15.6 percent and NPL ratios around 2.7 percent over 2019-22.

- Half of the PLL countries were also found to have effective financial supervision and are SDDS subscribers.[25]

19. Qualification assessments have relied on staff judgment, guided by relevant qualification criteria, core indicators, and thresholds. Core indicators have not represented redlines, with mitigating factors considered when specific thresholds were not met[26] and alternative indicators used when the core indicator was not deemed appropriate. For example, while Chile's reserves were below the recommended 100 percent of the ARA metric at the FCL and SLL approval and reviews, several mitigating factors—such as Chile's reserves more than covering estimated potential short-term banks' needs, its sizable sovereign wealth fund, FX liquidity lines, and its flexible exchange rate—were considered. For Panama, a dollarized economy, an indicator other than the ARA metric was used to assess reserve adequacy in the context of the PLL qualification assessment. Besides, PLL qualification assessments were transparent in explaining the reason for which a country was not assessed as performing strongly in a particular qualification area. Both Panama and Jamaica, for example, were found not to perform strongly in the financial sector supervision owing to remaining weaknesses in AML/CFT and in data adequacy, as neither is an SDDS subscriber.

20. In general, qualification criteria have remained valid and fit for purpose in the current environment. The qualification criteria and framework have remained valid and nimble enough to navigate the current environment characterized by high levels of inflation and higher borrowing costs for member countries. In particular, the possibility of using judgment in the qualification

[24] Morocco's fiscal framework has strengthened substantially over course of its four successive PLL arrangements, with the introduction and steadfast implementation of the Organic Budget Law. The fiscal deficit narrowed by about 2½ percentage points of GDP over the 2012-2019 period, and significant progress was made in removing regressive fiscal subsidies. North Macedonia adopted in September 2022, ahead of its PLL approval, a new Organic Budget Law, including fiscal rules with deficit and debt limits, applying from 2025. Fiscal targets under the PLL are in line with the new Organic Budget Law.

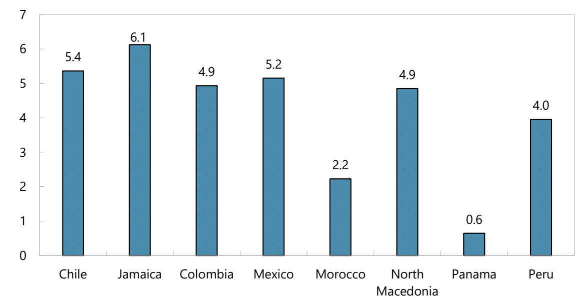
[25] Panama completed the three statistical-related structural benchmarks in its PLL which also contributed to bring Panama closer to SDDS subscription in some areas during the duration of arrangement, even though since the completion of the PLL some of Panama's progress was reversed due to capacity constraints.

[26] However, with respect to the FCL, significant shortcomings in one or more of these criteria—unless there are compensating factors, including corrective policy measures underway—would generally signal that the member is not among the very strong performers for whom the FCL is intended (see Adequacy of the Global Financial Safety Net: Review of the FCL, PLL and Proposals for Toolkit Reform, SM/17/140, paragraph 20).

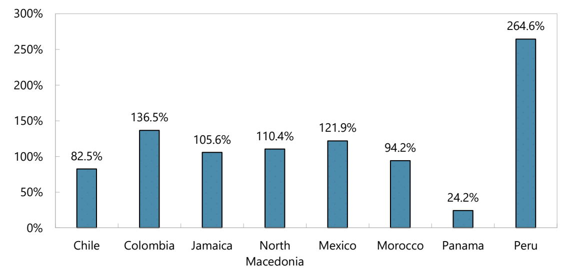
assessment to allow for a temporary deviation of inflation from target, for example, provided policies are in place to ensure convergence of inflation and inflation expectations anchored, has permitted countries to still qualify while having higher than single digit inflation, as the drivers of higher inflation were assessed to be external and of temporary nature (see Colombia 2022 FCL midterm review,[27] for example).

Figure 5. Qualification Assessment

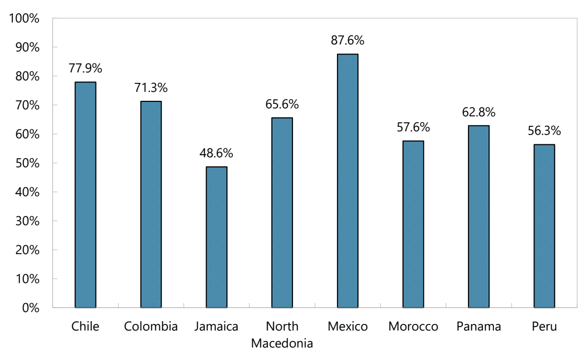
Inflation, average 2019-22 (percent)



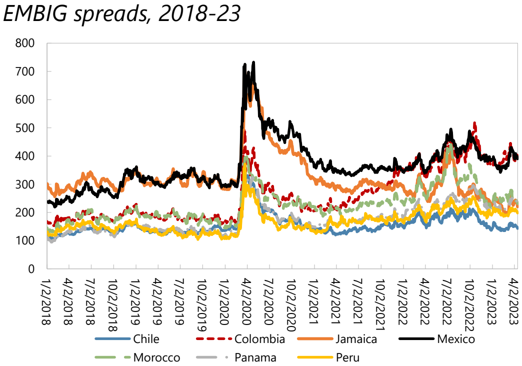
Reserves in percent of ARA metric, average 2019-22



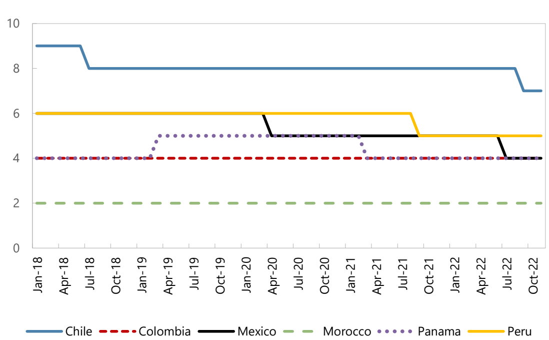
Share of private flows in total capital flows (percent)



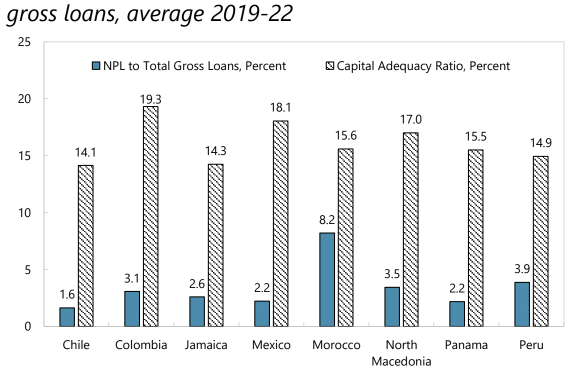
EMBIG spreads, 2018-23



Credit ratings (Moody's LT foreign currency rating, 2018-22)



Regulatory capital to risk-weighted assets and NPL to gross loans, average 2019-22



Sources: World Economic Outlook, Bloomberg, Moody's rating reports, World Development Indicators, and IMF staff calculations.
Notes: EMBIG spreads as of April 14, 2023. Moody's rating as of November 1, 2022. For Morocco, capital adequacy and NPL ratios averaged over 2019-2022Q2 and 2019-2022Q3, respectively.

[27] Colombia: Review under the Flexible Credit Line Arrangement-Press Release; Staff Report; and Statement by the Executive Director for Colombia (IMF Country Report No. 23/150).

B. Debt Sustainability Analysis

21. In the context of precautionary arrangements, debt sustainability assessments need to be informed by the drawing scenario, in addition to the baseline, under any of the following three settings:[28]

(i) if the arrangement is subject to Exceptional Access (EA) policy;

(ii) if shocks that may trigger a drawing are not adequately captured by the medium-term Market Access Country (MAC) Sovereign Risk and Debt Sustainability Framework (SRDSF) modules; or

(iii) when review departments have doubts about the realism of the DSA baseline that cannot be resolved through discussions with the country team.

In practice, this has been implemented by basing the debt sustainability assessment on the mechanical signal obtained under the drawing scenario, when any of the three settings above holds in the context of precautionary arrangements.

22. Staff proposes that setting (iii) be amended. This setting would thus simply read: "when there are doubts about the realism of the DSA baseline." This revision makes clearer that the circumstance discussed in no way impinges on internal processes.

23. Staff also proposes a refinement of the procedure for debt sustainability assessments for precautionary PLLs. This refinement would help streamline the assessment of qualification, on the basis that PLL countries have sound fundamentals and policy frameworks. Staff proposes that the sustainability assessment of a precautionary PLL in settings (i) and (ii) above be informed by the mechanical signal for debt sustainability under the baseline scenario—which should be "sustainable with a HP"—and by whether debt is on a decreasing path or at least stabilizes towards the end of a 5-year horizon, under the drawing scenario (Table 1). The currently implemented requirement for debt to be sustainable with a HP under the drawing scenario in settings (i) and (ii) is too stringent given precautionary PLL qualifiers' sound economic fundamentals, institutional policy frameworks, and policies which are expected to help maintain debt sustainability in the drawing scenario.[29] While the proposed change could carry some modest risks given that debt stabilization in the adverse scenario could occur at a high level, it is unlikely to materially impact the quality or accuracy of staff's assessment since the country's strong policy reaction would generally increase its debt-carrying capacity while also keeping the debt level in check. In setting (iii), sustainability assessments

[28] Per the 2021 sovereign risk and debt sustainability framework (SRDSF) for market access countries and the Staff Guidance Note No. 2022/039.

[29] These features of the country—essentially strong policy reaction functions—should ensure that the debt ratio reverts. However, when the DSA is run on the drawing scenario, this implicitly imposes a "shock-on-independent shock" scenario, without accounting for any reversion. Thus, the current requirement for debt to be sustainable with a HP under the drawing scenario of EA PLLs is too stringent.

for the PLL would continue to use the drawing scenario.[30] The need to assess capacity to repay (CtR) in the drawing scenario constitutes an additional safeguard in all settings.

Table 1. Debt Sustainability Requirements for Precautionary FCL and PLL Arrangements

	Baseline scenario	Drawing scenario		
		FCL	PLL below EA	PLL with EA
Status quo	Sustainable with HP	Not tested*	Not tested*	Sustainable with HP (**)
Proposed refinement		Not tested*	Not tested*	Debt on a decreasing path or at least stabilizing over 5-year horizon

Notes: * The "Not tested" wording for the drawing scenario applies only in the absence of circumstances (i) and (ii) specified in ¶21 above and in the absence of circumstance (iii) under the proposed refinement. Highlighted cell indicates difference from status quo; HP=debt sustainable with high probability.
** The requirement of a public debt position sustainable with HP applies at approval of the PLL and is a core indicator for meeting the qualification criterion of sound public finances.

24. The debt sustainability assessment requirement for precautionary SBAs would remain unchanged. Under the three settings in ¶21, debt sustainability analyses for precautionary SBAs would need to be conducted fully on the drawing scenario, which would be the one determining the mechanical signal for debt sustainability. This procedure remains in line with current practice.

25. No changes are envisaged for precautionary FCLs either. The SRDSF guidance note defers to this review for clarifying the DSA requirements for FCLs under the disbursing scenario in the context of the instrument's qualification framework.[31] Staff proposes no changes for FCLs: since the FCL is carved out of the EA policy, circumstance (i) above (¶21) does not apply regardless of access. While circumstances (ii) and (iii) would require the drawing scenario to inform the debt sustainability assessment, they are considered very unlikely to occur for FCLs. The CtR assessment and, for large FCLs, the assessment of the impact of the arrangement on Fund liquidity would continue to play a primary role in ensuring that requested access levels are adequate and risks to Fund finances remain at acceptable levels.

26. The procedure described above reflects the confidence and policy safeguards provided by the qualification requirements for these types of arrangements. These requirements are most stringent for FCLs, where fundamentals, institutional frameworks, and policies are very strong, and least stringent for SBAs, leaving PLLs in an intermediate position in the toolkit.

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[30] Specifically, in assessing the requirement applicable for approval of a PLL which requires that the member has, at approval, a public debt position that is sustainable with a high probability in the medium term, as well as for the assessment of the qualification criterion of sound public finances, including a sustainable debt position, and for assessments under the exceptional access policy, staff will use the drawing scenario.

[31] See footnote 120 of the 2022 Guidance Note, which states that "[*the current Precautionary Review*] may address the question of whether to subject drawing scenarios in FCL or SLL arrangements to SRDSF tools."

C. Governance

27. Since the 2017 review, the Fund has adopted a new framework for enhanced Fund engagement on governance (the "2018 Governance Framework").[32] This framework aims to promote a more systematic, candid, and even-handed engagement with member countries regarding corruption vulnerabilities and governance weaknesses linked to corruption in the six state functions that are most relevant to economic activity. These functions are (i) fiscal governance; (ii) financial sector oversight; (iii) central bank governance and operations; (iv) market regulation; (v) rule of law; and (vi) AML/CFT.

28. Consideration could be given to aligning the assessment of institutional strength in the FCL/SLL/PLL qualification frameworks with the Fund's governance framework. Under the current qualification frameworks for the FCL/SLL and PLL, a country should be assessed to have a very strong or sound institutional policy framework for the FCL/SLL and the PLL, respectively. Indicators considered as complement of the assessment are policy cyclicality and effective response to shocks. With respect to the latter, the FCL and PLL operational guidance notes state that the Worldwide Governance Indicators (WGI) on government effectiveness and control of corruption could be used to inform staff judgment on the strength of policy frameworks.[33] Poor governance, including weak control of corruption, could weaken a country's institutional frameworks, deteriorate capital flow composition (e.g., away from FDI), undermine prospective BoP stability, and ultimately reduce a country's ability to respond to shocks.

29. Staff proposes for the qualification assessment to continue focusing on the strength of the institutions directly related to economic management and the ability of a country to respond to shocks but, going forward, rely instead on the Fund's internal and holistic assessment of corruption vulnerabilities and governance weaknesses linked to corruption. In particular, the assessment of government effectiveness and control of corruption will be based on staff's assessment under the 2018 Governance Framework, rather than the WGI. Under the Framework, staff conducts a systematic assessment to identify corruption vulnerabilities and governance weaknesses linked to corruption in the six state functions most relevant to economic activity. The assessments rely on quantitative and qualitative data sources, including indicators such as the WGI, complemented by the analysis of Fund staff and other international organizations. In this context, a member would generally not be considered a strong performer for the purpose of FCL qualification if the staff assessment, including in related Article IV Consultation staff report discussion,[34] where applicable, shows that the member has severe corruption weaknesses and

[32] The Review of the 1997 Guidance Note on Governance—A Proposed Framework for Enhanced Fund Engagement (April 2018) supplements the 1997 Guidance Note on the Role of the Fund in Governance Issues and draws from the 2017 Review of the Guidance Note – Preliminary Considerations.

[33] For more details on the current qualification frameworks, see the operational guidance notes for the FCL and PLL.

[34] Pursuant to the 2018 Governance Framework, Article IV consultation reports are expected to include a discussion of corruption vulnerabilities and governance weaknesses linked to corruption if a determination is made that governance vulnerabilities are sufficiently severe to significantly affect present or prospective balance of payments or domestic stability.

governance vulnerabilities linked to corruption. However, the mere discussion of corruption or governance vulnerabilities in an Article IV staff report will not by itself disqualify a member from accessing financing under the FCL or PLL, nor does it necessarily signify that governance weaknesses are severe. If the staff assessment, including in related Article IV staff report discussions, where applicable, indicate that governance and corruption vulnerabilities are significant while not severe, the confidential preliminary assessment note, the staff note for the informal Board meeting discussing the FCL/PLL request, and the staff report for the formal request of an FCL/SLL/PLL arrangement, or review of an FCL/PLL arrangement, would generally be expected to discuss compensating factors such as corrective policy measures already underway at the time of the request.[35] When addressing the identified vulnerabilities is of critical importance for achieving the goals of the program, the staff report for the PLL request would be expected to include commitment to such measures in the form of ex post conditionality, or prior actions where relevant.

D. AML/CFT

30. The treatment of AML/CFT weaknesses in FCL and PLL arrangements has varied. Vulnerabilities in the AML/CFT framework, as evidenced in cases of "grey listing" by the Financial Action Task Force (FATF),[36] may present risks to financial sector soundness and signal weaknesses in institutional frameworks, particularly supervision.[37] However, the core qualification criterion of "effective financial sector supervision" does not currently explicitly discuss AML/CFT issues. To date, no country approved for FCL support has been on the FATF grey list at the time of approval.[38] But three countries were approved for a PLL arrangement while on the grey list (Panama in 2021, Morocco in 2012, Jamaica in 2023), and the treatment of grey listing in the assessment of qualification criteria and in setting ex post conditionality have varied across these countries. Panama was on the grey list when it requested a PLL arrangement but delays in implementing conditionality on exiting the grey list resulted in a six-month delay in completing the second review under the arrangement. Morocco was on the grey list when it requested its first PLL arrangement in 2012, but its grey listing did not come under scrutiny in the qualification assessment, and Morocco was not subject to ex post conditionality in this area. In contrast, Jamaica's PLL arrangement was approved in 2023 while Jamaica was on the grey list, with a structural benchmark on AML/CFT. This checkered experience shows the need for clearer guidance on how AML/CFT weaknesses should inform qualification for an FCL, PLL, and SLL arrangement—to avoid the perception of differing treatment across countries and avoid reputational risks to the Fund (e.g., risks of not taking this area into

[35] Compensating factors could be spelled out in the written communication.

[36] FATF "grey listing" refers to countries under increased monitoring overseen by the FATF International Cooperation Review Group. See more here.

[37] It should be noted that grey listing is not the only indicator for strategic deficiencies in AML/CFT supervision.

[38] Morocco's FCL arrangement was approved in 2023 shortly after its exit from the FATF grey list. For the classification assessment, the strengthening of the AML/CFT framework that led to Morocco being removed from the FATF grey list in February 2023 was considered to have mitigated any strategic deficiencies on AML/CFT that existed during the previous five years

account in the qualification assessment while it is an important aspect of the country's financial sector supervision, or the risk of providing uneven coverage across countries).

31. The review proposes to formally integrate AML/CFT issues into the "effective financial supervision" criterion of the qualification framework and clarify that FATF grey listing does not in itself disqualify a member for an FCL, PLL, or SLL. The review will clarify that AML/CFT issues, including FATF grey listings, are integrated into staff's assessment of "effective financial sector supervision." The bottom-line assessment of the "effective financial sector supervision" criterion will consider relevant existing indicators (i.e., FSAP findings, assessment of legal and institutional framework and operational capacity for prompt corrective actions and emergency assistance). As is the case currently, a FATF grey listing would not automatically disqualify a member for approval of an FCL/PLL/SLL or for completion of reviews under these arrangements. In the event of such listing, a case-specific assessment by staff would be required to ascertain whether the deficiencies suggest that the "effective financial sector supervision" criterion is not met.[39] Such assessment would look at how deep and persistent AML/CFT weaknesses are, as well as the substantive aspects of the FATF listing and the country's action plan related to effective supervision. Staff should avoid solely relying on FATF determinations, as cross-conditionality is prohibited, and should be making its own judgement including through using in-house resources, such as FSAP and Article IV reports. Nonetheless, staff's judgement would still need to be guided on technical issues by the FATF standard and methodology, which have been endorsed by the Board[40] (and how they have been applied in FATF assessments), to ensure methodological transparency and evenhandedness. Serious strategic deficiencies in the AML/CFT framework relevant to financial sector supervision would generally indicate that a country has remaining vulnerabilities that are relevant for qualification purposes, with severe vulnerabilities normally suggesting that the country does not have very strong institutional policy frameworks to qualify for an FCL arrangement.[41] Under PLL arrangements for countries with AML/CFT weaknesses relevant to financial sector supervision, the member would generally be expected to commit to strengthening the AML/CFT framework, likely supported by structural conditionality.

[39] For example, members may be FATF-listed while having minor outstanding weaknesses; others may have major AML/CFT weaknesses as evidenced by a full catalog of action items that remain unaddressed (though only elements related to financial sector supervision could potentially affect staff's assessment of the member's qualification). The Guidelines on Conditionality inform program design in PLL arrangements, including with FATF listed countries with action plans, and hence, the full range of items under FATF action plans are not necessarily included in Fund conditionality in a PLL arrangement where the measures are not considered critical to achieve program objectives, or for other reasons (e.g., fall outside the program period, are outside the Fund's expertise or mandate, are not in line with parsimony, etc.). In addition, the absence of grey listing does not in all cases imply that there are no AML/CFT issues that could undermine effective financial sector supervision, as these can be identified in an assessment without necessarily leading to a grey listing (which requires strategic shortcomings in several areas).

[40] See *IMF Executive Board Reviews the Fund's Strategy for Anti-Money Laundering and Combating the Financing of Terrorism*, April 11, 2014, PR 14/167.

[41] See paragraph 20 of SM/17/140: "Very strong performance against all qualification will not be necessary to secure qualification under the FCL. However, significant shortcomings on one or more of these criteria—unless there are compensating factors underway—would generally signal that the member is not among the strong performers for whom the FCL is intended."

ADEQUACY OF THE TOOLKIT

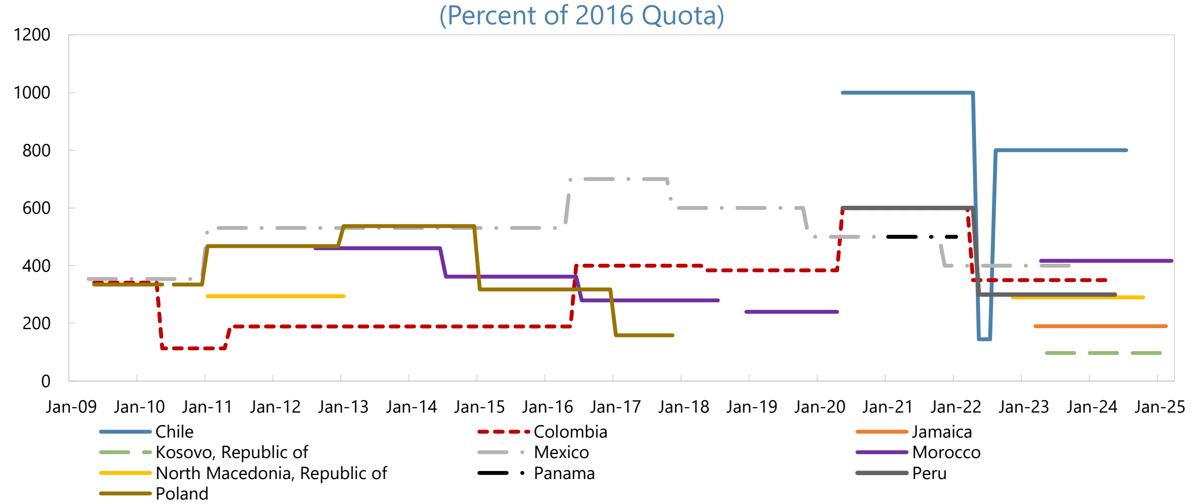
This section assesses the adequacy of the instruments to address shocks in the current environment and proposes: (i) dropping exit expectations for low-access FCLs; (ii) raising PLL access limits; (iii) raising SLL access limits; and (iv) adding explicit provisions on concurrent use of FCL and SLL.

A. Developments in Access Levels

32. **Since the 2017 review, access levels in FCLs and PLLs have generally decreased** (Figure 6). Mexico and Colombia, FCL users since 2009, have both reduced access under successive FCLs since 2017 (from 700 to 400 percent of quota and from 400 to 350 percent of quota, respectively). Peru halved its access under the FCL from 600 percent of quota in 2020 to 300 percent of quota in 2022 and declared its intention—external risk permitting—to exit the FCL when the current one expires. Chile temporarily exited the FCL (1,000 percent of quota) and transitioned to an SLL arrangement (145 percent of quota), shifting back to a new FCL arrangement (800 percent of quota) as external risks re-emerged a few months later, highlighting the flexibility of these instruments. All in all, over the last five years, average access under the FCL has declined from 550 to 463 percent of quota.

Figure 6. Access Under FCL, SLL and PLL Arrangements 1/

(Percent of 2016 Quota)



Sources: Financial Data Query, and IMF staff calculations.
1/ This chart shows cumulative access over the period of the arrangement for PLLs.

33. **Adverse scenarios developed to justify PLL and FCL access have been underpinned by comparable shocks for different countries, with consistent assumptions over time.** Recent staff reports have reported detailed assumptions behind the adverse scenarios, often transparently in a table (Chile, Peru, Panama, Morocco) and compared them to those in previous arrangements

(Colombia, Chile). Shocks to fuel prices, FDI, and debt rollover remain the most used shocks (Table 1).[42] Overall, shocks to fuel prices and private short-term debt rollover tend to be the most severe when compared to historical shocks, while shocks to public medium-term debt are generally assumed to be less severe, likely reflecting lower perceived risks to long-term financing for the general government. Also, financial account shocks contribute the most to the overall shock (72 percent of the overall shock before reserve drawdown, on average), while current account shocks contribute to a lesser extent. For each country, shocks have tended to stay in the same percentile range from one arrangement to the other. There does not seem to be much evidence of shocks to the current account and capital flows being less severe, as shares of the baseline, in 2022 or 2023 compared to previous years, likely implying that the level of perceived external risks is still significant even after the pandemic and Russia's invasion of Ukraine shocks.

Table 2. Severity of Shocks Relative to Kernel Distributions

	Morocco		Colombia 1/			Mexico		Peru		Chile		Panama	North Maced.	Jamaica
Year	2018	2023	2018	2020	2022	2019	2021	2020	2022	2020	2022	2021	2022	2023
Arrangement	PLL	FCL	FCL	FCL	FCL	FCL	FCL	FCL	FCL	FCL	FCL	PLL	PLL	PLL
Access (% of quota)	240	417	384	600	350	500	400	600	300	1000	800	500	290	190
FDI	Orange	Orange	Orange	Orange	Orange	Orange	Red	Red	Orange	Orange	Orange	Red	Green	Orange
Fuel price	Green	Green	Red	Red	Red	Gray	Gray	Red	Gray	Red	Red	Gray	Green	Green
Public ST debt rollover	Orange	Gray	Orange	Orange	Orange	Orange	Orange	Gray	Gray	Gray	Gray	Gray	Gray	Gray
Private ST debt rollover	Green	Red	Red	Red	Red	Red	Red	Red	Red	Red	Red	Red	Red	Gray
Public MLT debt rollover	Green	Green	Orange	Orange	Gray	Orange	Orange	Green	Green	Gray	Gray	Green	Gray	Orange
Private MLT debt rollover	Orange	Orange	Red	Red	Red	Orange	Orange	Orange	Orange	Orange	Orange	Red	Gray	Gray
Contribution of the financial shock to overall shock (before reserve drawdown)	31%	61%	70%	73%	77%	96%	93%	78%	73%	92%	98%	77%	68%	21%

1/ Colombia 2020 column corresponds to the augmentation Staff Report.

Notes:

Colors denote the severity of the shock compared to the Kernel distribution. Red: shock below the 25th percentile of historical shocks; Orange: shock between the 25th percentile and the median; Green: shock above the median historical shock under the Kernels. Cells are gray if the specific shock is not apply for the country.

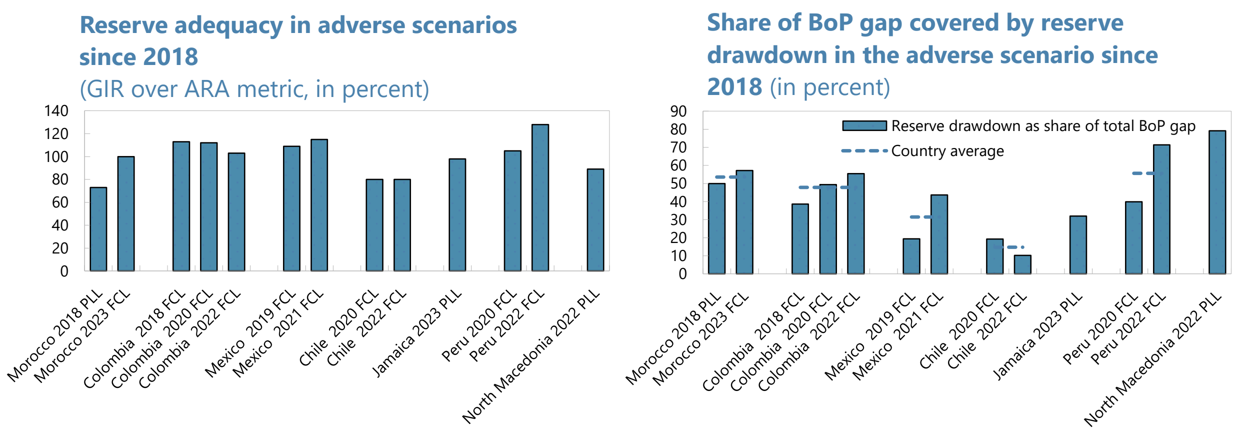
Shocks to the fuel price will have different effects depending on whether the country is a net fuel exporter or importer. E.g., a drop in the fuel price as observed in 2020 had negative/positive consequences for net fuel exporters/importers, while a fuel price surge as observed in late 2021 and early 2022 had positive/negative consequences for net fuel exporters/importers. This explains why the fuel price shock can be signaled as milder through this color coding for some countries, for which a negative shock on the oil balance would result from an increase in oil prices. Adverse scenario shocks are also drawing on the WEO adverse scenarios, when it comes to fuel prices, for example, which can also drive the severity of the assumed shock.

34. **The External Economic Stress Index (ESI) continues to inform access and exit discussions under FCL and PLL arrangements** (Annex VI). An assessment of FCL and PLL arrangements approved since the 2017 Review suggests that the ESI captures similar sources of external risks within and across arrangements—namely, risks to exports and financial flows—with weights on proxy variables reflecting differences in country characteristics and exposure to external stress. For instance, risks to equity and debt portfolio investment flows account for 45 to 50 percent

[42] Not all countries are applying shocks to all the variables above, based on country specificities. The Chile adverse scenario, for example, assumed full rollover of public sector external debt, given the limited public external financing needs compared to the large size of public liquid assets.

of the ESI for Colombia, Chile, Mexico, and Panama, consistent with their well-developed financial markets, while growth developments in the Euro area drive the bulk of the ESI for Morocco given strong trade, remittances, tourism and FDI ties. There is also evidence that improvements in the ESI (i.e., lower external risks as indicated by the index) are associated with reductions in access, while increased risks correlate with higher or unchanged access levels. For instance, Mexico's request for a lower access in 2021 relative to 2019 was consistent with reduced external risks signaled by the ESI, while Colombia's augmentation of access shortly after the approval of the 2020 FCL arrangement was in line with a sharp worsening of the ESI. The construction of the ESI has been broadly aligned with best practices since the 2017 Review, with comparability of the ESI shock scenarios across countries improving thanks to the systematic use of the latest WEO downside scenario, GFSR, or G-RAM for constructing the ESI. No further enhancements in the ESI seem warranted at this stage, although flexibility under current guidance could be better leveraged: while selected arrangements have highlighted limitations of the ESI, these could be addressed through updates to proxy variables and/or weights consistent with existing guidance (Annex VI).

Figure 7. Reserve Buffers in Adverse Scenarios



Sources: Country Staff Reports, and IMF staff calculations.

35. **Access considerations have also been guided by the availability of buffers to mitigate those risks and the authorities' risk tolerance** (Figure 7). Since 2019, except in the case of Chile, adverse scenarios for FCL access have gradually assumed that a higher share of the financing gap would be covered by a reserve drawdown. This trend has not been accompanied by a deterioration in the level of remaining reserves after reserve drawdown (in the adverse scenario). In most countries, the 80 percent threshold has remained a floor for the reserve coverage in the adverse scenario. For Colombia, Mexico and Peru, the higher reserve drawdown in the adverse scenario compared to previous arrangement—with a commensurately lower FCL access—could reflect a shift in the authorities' views on optimum self-insurance.

B. FCL Use Under Protracted Risks

36. While elevated global risks argue for uninterrupted access to help members address potential BoP difficulties and buttress global financial stability, concerns related to prolonged use also need to be considered. Some FCL users (Mexico and Colombia) have benefitted from prolonged use of their FCL, for more than a decade by now. The membership remains divided on the merits of prolonged use of the FCL, with different views expressed at the 2017 Review of the FCL and PLL:[43] some Directors have repeatedly expressed concerns about successive FCL arrangements and underscored the need for exit strategies, while others have argued that they should serve as an uninterrupted umbrella policy. An additional complication arises if countries' economic fundamentals gradually deteriorate over time, but disqualification and discontinuation of the FCL could trigger adverse market reactions. Economic arguments could cut both ways. On the one hand, prolonged use could relieve countries from accumulating excessive costly reserves, provide some stability when it comes to the level of available buffers, and be relevant particularly in contexts of elevated external risks with limited alternative sources of liquidity support. It could also help limit spillovers and reduce systemic risks. On the other hand, prolonged use would potentially lock in Fund resources that could otherwise be used to support the resolution of actual BoP needs elsewhere and may disincentivize countries to strengthen their own resilience to external shocks. Promoting exit from the FCL, on the contrary, could incentivize countries to further increase their resilience with good policies, going beyond accumulation of reserve buffers.

37. This review reiterates that any reduction in access under, and exit from, FCL arrangements should continue to be state-, rather than time-, dependent and considers three possible options to address exit expectations.

- **Option 1.** *Encourage reduction in access or exit from precautionary FCL arrangements only when access exceeds 200 percent of quota and if external risks have abated.* Offering low-access precautionary FCL arrangements without explicit exit expectations[44] could offer an uninterrupted umbrella policy (consistent with residual risks), while avoiding committing large amounts of Fund resources for an extended period. For FCL arrangements with access exceeding 200 percent of quota, exit—including through a gradual reduction in access, provided that external risks abate—would continue to be strongly encouraged. FCL users retain the option of

[43] "[Most] Directors remained concerned about the prolonged use of high-access precautionary arrangements and thus saw scope for strengthening price-based incentives. Many of them saw merit in introducing time-based commitment fees, some favored steepening the commitment fee structure to discourage unnecessarily high precautionary access, and a few saw scope for a combination of both options. Some other Directors reiterated that exit should continue to be state-dependent and did not see a case for stronger price-based incentives." (BUFF/17/54, July 10, 2017)

[44] Currently, the authorities' exit prospects would be expected to be included at the time of the initial FCL request. Such exit strategy would be expected to include the following elements: (i) a statement about exit contingent on reduction of external risks; (ii) a statement regarding any efforts the authorities intend to take to improve domestic resilience; and (iii) a statement on the expectation that access will decline in successor arrangements when the right conditions are in place. Under Option 1, an exit strategy would not be required at the time of the FCL request but would be expected if access is augmented during the arrangement period and exceeds 200 percent of quota.

requesting an augmentation of access if warranted by developments in external risks, subject to continued qualification and capacity to repay. Qualification would be assessed at each request or review under the arrangement, and the level of access would similarly need to be justified through staff analysis as noted above.

- **Option 2.** *Revisit the structure of level-based commitment fees of the FCL—when accessed on a precautionary basis—to better incentivize exit from high access FCLs.* The current precautionary FCL commitment fee increases with the level of access available over a twelve-month period (see text chart).[45] Options to further disincentivize high access FCL arrangements could include (i) adding a new step in the access scale (at, say, 800 percent of quota), with higher fees above it, or (ii) increasing the quantum of fees associated with each level step of the already existing structure (Table 3). These changes to commitment fees, however, would apply to all arrangements in the credit tranches (and not just the FCL) approved in the future, given legal requirements of uniformity of charges.[46]

Table 3. Commitment Fees Applicable to Precautionary Arrangements

	Commitment Fees
FCL	**Refundable upon disbursement** 15 bps up to 115% quota, then 30 bps up to 575% quota, then 60 bps above 575% quota
PLL	
Prec. SBA	
SLL	**Non-refundable** 8 bps

- **Option 3.** *Reconsider time-based FCL commitment fees.*[47] This option is explored further below and in Annex VIII. While this option would incentivize exit, it would also make exit time- rather than state-dependent. The legal requirements of uniformity of charges, as mentioned for Option 2, would also apply.

38. In staff's view, dropping exit expectation for low-access precautionary FCL arrangements (Option 1) strikes a balance between disincentivizing excessive use of precautionary instruments and members expressed need for a minimal umbrella policy in uncertain times. In staff's view, options 2 and 3 would unduly reduce the usefulness of the FCL at the current juncture of elevated global risks and would apply to all other GRA instruments. Option 3 would also go against the intended objective of the instrument by making exit time dependent. Lifting—or at least reducing—exit expectations for low-access precautionary FCL arrangements (Option 1) reconciles the need to incentivize exit with the need to maintain some predictability amid high uncertainty.

[45] Once drawn, FCL credit outstanding is subject the same charges and surcharges as other GRA facilities.

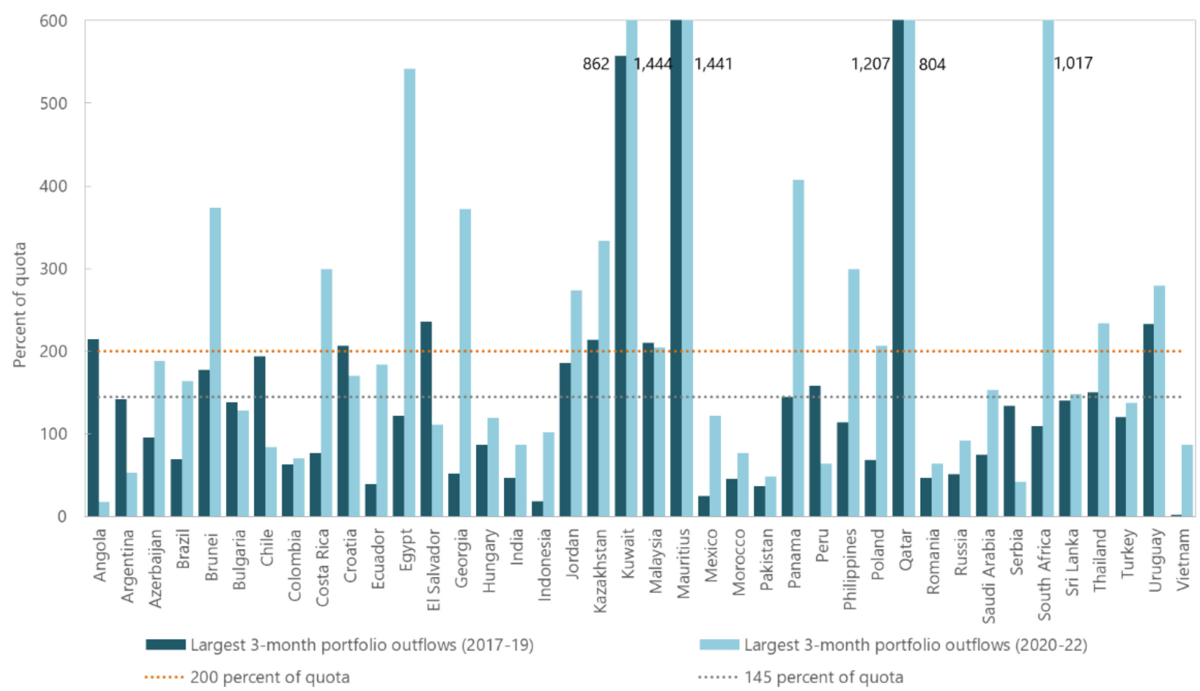
[46] The commitment fee is a form of charge under the Articles of Agreement and, as such, is required to be uniform for all members (Article V, Section 8(d)). Differentiation of charges has been limited to relevant differences in members' use of the Fund's resources (e.g., having a different balance of payments need as addressed by a special facility).

[47] Time-based commitment fees were discussed in the 2017 Review of FCL and PLL, and ultimately rejected by the Executive Board. See footnote 50 above.

C. Access Level and Concurrent Use of the SLL

39. Several factors could explain the limited interest in the SLL so far. As noted, Chile has been the only user of the SLL since its establishment in April 2020. *First*, the access limit of the SLL, at 145 percent of quota (or 2.1 percent of GDP on average for EMEs), is considerably smaller than the average size of BSLs extended to EMEs (3.1 percent of GDP). *Second*, the pandemic gave rise to tail risks associated with large potential BoP needs, which were thought to be better addressed by the FCL rather than SLL. *Third*, given its novelty, potentially qualifying countries may not have been fully aware of the SLL's benefits. It may therefore be worth exploring whether an increase in the SLL access limit and/or concurrent use with the FCL could make the SLL more attractive, mindful of its role within the current Fund toolkit and considering implications for Fund resources.

Figure 8. Large Portfolio Outflows vs. IMF Normal Access Limit 1/



1/ Bars represent largest quarterly outflows during the period 2017Q1–2022Q4. Sample includes 40 countries with the largest outflows in USD during 2017–22 among 91 countries surveyed.

40. Against this background, staff proposes to retain the SLL in the Fund's toolkit and proposes options to enhance its design.[48]

- **Option 1.** *Raise the access limit under the SLL to 200 percent of quota.*[49] The higher access under the SLL would be permanent and would acknowledge that capital flows, as well as the moderate and short-term BoP needs covered by the SLL, have become larger in a complex global environment (Figure 8). This would make SLL access more comparable to financing under the BSLs and could increase the SLL's usefulness as an exit instrument from the FCL, as suggested by some survey respondents (Annex VII). Raising SLL access *beyond* 200 percent of quota, on the other hand, may not be advisable, as it would concentrate large repayments within the short 12-month repurchase period of the SLL, with a likely need to revisit some of the features of the instrument specifically linked to the "special, short-term, moderate BoP need" it is meant to address (e.g., the revolving aspects and lower fees).[50]

- **Option 2.** *Explicitly provide for concurrent use of the SLL with the FCL.*[51] At the time of its inception, the SLL was viewed to be redundant if used concurrently with the FCL, as the latter can cover any large potential BoP needs, while the SLL is only meant to address potential BoP needs arising from moderate short-term capital account pressures.[52] But Chile's experience illustrates the possibility of the two BoP needs co-existing, as tail shocks of uncertain size (addressed by the FCL) could have a short-term component, as uncertainty triggers moderate

[48] Without a decision by the Board by 2025 to extend the SLL, it is due to sunset seven years after its inception (in 2020).

[49] On March 6, 2023, the Executive Board approved an increase in the GRA cumulative access limit from 435 to 600 percent of quota and the annual access limit from 145 to 200 percent of quota for a period of 12 months to better support the membership in a highly uncertain environment. See staff paper [Temporary Modifications to the Fund's Annual and Cumulative Access Limits](). Access under the SLL is carved out from the access limits set forth in the policy on overall access to the Fund's resources in the General Resources Account. However, outstanding amounts under the SLL count towards such access limits if a member requests access to Fund resources under another Fund facility.

[50] The SLL Board paper (IMF COVID-19 Response—A New Short-Term Liquidity Line to Enhance The Adequacy Of The Global Financial Safety Net) is silent on the DSA issue, and states, "The proposed process for the approval and use of an SLL arrangement largely follows the process for FCL arrangements, with two notable differences: the extension of an "offer" by the Fund to those members that qualify, and the absence of a prior informal Board meeting. The main steps are the following, with operational modalities to be clarified further in a staff guidance note." In the event, a guidance note was not produced. The Chile SLL request involved a streamlined CtR assessment, the absence of an adverse scenario, and the carve out for a DSA assessment under the disbursing scenario. The access level was justified and calibrated by analyzing historical capital account shocks without recourse to an adverse scenario (required for PLL and FCL requests), and by making a case that access under the SLL would be sufficient to cover most of historical shocks. The CtR analysis was streamlined, focusing on short-term liquidity risks.

[51] The 2020 SLL paper states, "[g]oing from an FCL arrangement to an SLL arrangement, or vice-versa, would require cancelling the existing arrangement (FCL or SLL, respectively) and requesting a new arrangement (SLL or FCL, respectively)." This was intended to clarify that a transition from one instrument to the other would not be automatic. However, to the extent the statement disfavors concurrent use, this is a policy consideration rather than a legal preclusion.

[52] More specifically, the SLL deals with members with short-term balance of payments difficulties that: (i) are only of a potential nature, reflected in pressure on the capital account and the member's reserves; (ii) are resulting from volatility in international capital markets; and (iii) are reasonably expected to be limited in scale and to require, at most, fine-tuning of monetary and exchange rate policies.

capital outflows which could self-reverse once uncertainty dissipates.[53] While the FCL can cover this short-term component of BoP need, it may be better addressed by the SLL, an instrument expressly designed for that purpose. Concurrent use of the FCL and SLL would thus offer *complementary* insurance against both moderate and tail risks. It would also present the added advantage of (i) lowering the overall costs for a borrower that meets the FCL/SLL qualification requirements since the SLL is a special facility that has somewhat lower commitment fees than the FCL, (ii) providing FCL users with enhanced liquidity management options given revolving access under the SLL, and (iii) enhancing the attractiveness of the SLL by addressing concerns about its relatively low level of access. Concurrent access should not have a large implication for the demand for Fund resources and the Fund's forward lending capacity, provided there is rigorous analysis to ensure that the level of combined access reflects the size of a member's total potential BoP need (i.e., the SLL would not be a "top up").

41. Staff proposes pursuing both options 1 and 2. The survey of country authorities points to both a concurrent use of the SLL with the FCL and higher access under the SLL as the most-preferred policy changes that could make the SLL more useful (Annex VII). Taken together with the proposal to introduce exit-free low-access precautionary FCL arrangements, options 1 and 2 would afford users enhanced flexibility under various scenarios. For instance, a country with a large FCL access could, commensurate with the decline in risks, reduce access to 200 percent of quota and, at the same time request an SLL arrangement with 200 percent of quota as part of its exit strategy (provided it faces the special BoP need under the SLL), thus benefitting from a total access (or "umbrella insurance") of 400 percent of quota without exit expectations. If the special BoP need covered by the SLL were to materialize, the country could draw on the SLL portion and reconstitute access within 12 months, thanks to the SLL's revolving feature, while continuing to be covered by insurance provided by the FCL.

42. Staff proposes to treat the low access exit expectation free FCL, and the SLL as a package, as they could reinforce each other. Removing exit expectations for FCLs with access not exceeding 200 percent of quota need not undermine SLL use, since the latter has specific benefits that make it more adapted to short-term moderate BoP needs compared to the FCL, namely the lower fees and revolving feature, which means that SLL access could be reconstituted after drawdown. Vice versa, a 200 percent of quota SLL would not necessarily be a substitute to a low access exit expectation free FCL, as the FCL, in contrast with the SLL, could be used in situations where a longer repayment period is needed. The country could therefore use both concurrently and would have the choice to decide which one to draw depending on the situation—SLL for liquidity management purposes versus FCL for longer lasting shocks, for example. Both would be complementary. In any case, any request for concurrent use would have to be justified by potential BoP needs whose total amount is commensurate to the size of the total access requested under both instruments.

[53] For example, in the case of Chile, the tail shock was the large drop in copper prices. However, early in the shock, it was difficult to foresee how low prices would fall, and how large the medium-term BoP need would be. This triggered a short-lived capital outflow episode.

43. Separately, an option of synchronized SLL offers could incentivize optimum use of the instrument. In the event of worsening global economic conditions, synchronized access by several countries could help reduce the stigma of being the first mover to request financial assistance from the Fund. A synchronized extension of SLL offers to, and opt-ins by qualifying members, could help strengthen the effectiveness of the response to a common shock and, possibly, encourage additional take-up by other members. The process could be similar to the one envisaged earlier for a synchronized approval of FCLs (although this possibility has not been used so far).[54]

D. Maintaining the Role of the PLL

44. At this juncture, the PLL continues to have an important role in the lending toolkit. Many of the arguments presented in favor for eliminating the PLL in the 2017 review—the sense of tiering vis-à-vis the FCL, little comparative advantage relative to a precautionary SBA, and the broader objective of limiting a proliferation of instruments—continue to apply. However, recent renewed interest in the PLL (from North Macedonia and Jamaica) and the tightening of global financial conditions argue against its elimination at this time. The survey results also support maintaining the PLL in the Fund's lending toolkit, underscoring the PLL's perception as a graduation instrument from the SBA as one of its key attractive features (Annex VII).

45. Increases in the PLL annual limit on access at approval and the PLL instrument access cap could be warranted. Since its creation in 2011, the PLL annual limit on access at approval has remained at 250 percent of quota and the access cap that applies to all PLL arrangements at 500 percent of quota, thereby implying an erosion of access relative to GDP levels. Besides, PLL access has been cited in the member survey as one of the top reforms that could enhance the instrument's effectiveness. Finally, while a cap on the PLL is consistent with the countries still having remaining vulnerabilities (in contrast with FCL countries, which have very strong fundamentals and therefore access to the uncapped FCL, provided BoP needs justify it), this can be seen as being inconsistent with the precautionary SBA, which is uncapped.

46. In this context, the review proposes to raise permanently the limit on access at approval for PLL arrangements and the PLL instrument access caps by 20 percent from current levels (**Table 4**). Specifically, the annual limit that applies at approval of a *one to two-year PLL arrangement* would be raised from the current 250 to 300 percent of quota. In addition, the access cap that applies cumulatively to *all PLL arrangements* (regardless of their duration) would be increased from 500 to 600 percent of quota. Furthermore, for *6-month PLLs*: (i) the per arrangement limit would be raised from the current 125 percent of quota, to 150 percent of quota; (ii) the exceptional per arrangement limit would be raised from the current 250 percent of quota, to 300 percent of quota; and (iii) the overall 6-month PLL instrument access cap would be increased from the current 250 percent of quota to 300 percent of quota (see table below summarizing proposals). All in all, staff proposes to increase the PLL specific annual limit at approval and PLL instrument

[54] See the Flexible Credit Line Operational Guidance Note, Annex VII, based on Technical Note on Synchronized Approval of Flexible Credit Lines for Multiple Countries; IMF Policy Paper; November 12, 2010.

specific caps by proportionately less than the recent temporary increase in the GRA access limits.[55] Exceptional access policy would continue applying to PLL arrangements with access exceeding the normal annual and cumulative GRA access limits.

Table 4. Access Approval Limits and PLL Instrument Caps (Percent of Quota) 1/

	1–2-year PLLs		6-month PLLs		
	Annual limit at approval	**Instrument Cap** (for all arrangements, regardless of duration)	**Standard per Arrangement limit**	**Exceptional per arrangement limit**	**6-month PLL instrument cap**
Status quo	250	500	125	250	250
Proposal	300	600	150	300	300

Notes: Access limits net of scheduled PLL repurchases. The per-arrangement access limit for 6-month PLLs is subject to a higher limit of 250 percent of quota in exceptional circumstances where the member is experiencing or has the potential to experience larger short-term BoP needs due to the impact of exogenous shocks, including heightened regional or global stress conditions.
1/ The PLL is also subject to the annual and cumulative limits in the GRA. The PLL instrument cap of 500 percent of quota (currently) applies for all PLL arrangements, including 6-month PLLs.

E. Use of the Precautionary SBA

47. The precautionary SBA has been a useful instrument for signaling countries' commitment to credible policies and macroeconomic stability. Case studies of recent users of the precautionary SBA show that the instrument has been a critical anchor for macroeconomic policies and reforms, supporting important progress in areas such as fiscal and external sustainability, monetary policy modernization, financial sector resilience, and governance. Survey respondents also agreed that the precautionary SBA provides a credible commitment mechanism with strong policy signaling to donors and investors, thus contributing to reducing sovereign borrowing costs, catalyzing external financing, and strengthening reserves (Annex VII). This is illustrated by the experience of Honduras, where reform implementation under successive precautionary SBA/SCF arrangements improved market confidence and attracted financing from donors and international markets, as evidenced by successful bond placements during the program periods (Annex IV).

48. Country experience also shows how precautionary SBAs have flexibly catered to users' needs in difficult times (Annex IV). The arrangements for Armenia, Georgia, and Serbia were all approved in 2022, in the context of high uncertainty to insure against, *inter alia*, shocks stemming from the war in Ukraine, while the 2019 SBA/SCF in Honduras was meant to cover BoP needs potentially arising from a negative terms-of-trade shock given the country's vulnerability to commodity price swings. The SBA in Serbia was designed to be hybrid, addressing an actual BoP need at approval and during the first year of the program, and a potential need during the second

[55] Applying the 38 percent increase enacted by the March 2023 temporary increase in GRA access limits to the PLL access limit at approval of an arrangement would raise such limits to 345 and percent of quota and would raise the PLL instrument cap to 690 percent of quota.

year. Serbia, Armenia, and Georgia continue to treat their SBA as precautionary as of May 2023 (after a first purchase made at approval for Serbia), and both Armenia and Honduras benefitted from a rapid access to Fund resources under their 2019 arrangements following the emergence of actual BoP needs at the onset of the COVID-19 crisis. In May 2023, the Executive Board approved a precautionary SBA for Kosovo, together with an RSF. Target recalibrations, program extensions, as well as access augmentations and rephasing—twice for Honduras, to support the authorities' pandemic response and help finance increased BoP needs associated with reconstruction efforts following climate shocks—showcased the flexibility of the SBA and SCF in managing large shocks within the perimeter of a UCT-quality program, obviating the need to seek emergency financing in difficult times. The survey results echo these attractive features of the instrument, with respondents appreciating the SBA's use on a precautionary or disbursing basis depending on the BoP need, its flexible duration, uncapped access, and absence of ex ante conditionality that normally makes it accessible to all Fund members (Annex VII). Reflecting this, at the conclusion of this review, staff plans to undertake outreach on precautionary instruments, underscoring the important role played by precautionary SBAs.

PROCEDURES AND OTHER POLICIES

To respond to new requests for precautionary arrangements in an agile manner, staff proposes procedural changes to simplify the process faced by the member, staff, and the Executive Board.

A. Overall Board Procedures

49. The review proposes three complementary reforms to reduce the number of Board discussions associated with FCL and PLL approvals and reviews:

- **Reform 1.** *Drop the requirement for an informal Board meeting for successor FCL and PLL arrangements.* For a successor FCL/PLL arrangement requested and considered by the Executive Board within three months of expiration of a successful previous FCL/PLL arrangement (i.e., an arrangement that was not cancelled and with no delays in the completion of reviews and, in the case of the PLL, also with no delays in implementation of ex post conditionality), the requirement of an informal Board meeting could be dropped, provided that, in staff's assessment, the country's fundamentals and external risks have not changed significantly since the last review. The logic is that the regular review of a member country in the context of the previous arrangement reduces the need for a prior informal discussion of the successor arrangement, and it increases likelihood that the member will continue to qualify. The Board would review qualification at the time of the Board meeting to consider the request for the successor FCL or PLL arrangement.

- **Reform 2.** *Encourage, where feasible, holding same-day back-to-back Article IV and informal Board discussions for FCL and PLL requests.* The FCL and PLL operational guidance notes recommend holding Article IV Board discussions at least 4 to 6 weeks prior to a formal Board meeting for either the approval of, or review under, an FCL or PLL arrangement to ensure the Board's appraisal can be incorporated in the staff report sent for review and management clearance.[56] In practice, the interval between has often been shorter, less than three weeks apart in many cases. The approval of an FCL or PLL arrangement thus requires holding three Board meetings within a very short period—an Article IV Board discussion, followed by an informal Board, and then a formal Board meeting—which creates administrative and timing pressures for staff and the Board. The option of holding the Article IV and the informal Board discussion back-to-back on the same day for FCL or PLL requests whenever possible, followed by a formal Board discussion two to four weeks later, would leave enough time to incorporate the Board's view on the Article IV consultation into the FCL or PLL formal request. With the Article IV staff report already presenting staff's up-to-date assessment of recent developments and policies, the staff note for the informal Board would be expected to be concise and to focus on FCL- and PLL-related issues: assessment of qualification, the member's actual or potential need for Fund resources and, for FCL requests, the impact of the arrangement on Fund liquidity, when access exceeds 575 percent of quota or SDR 10 billion (whichever is lower), as required by the FCL policy.

- **Reform 3.** *Encourage, where feasible, holding a single Board meeting for the Article IV Consultation and the FCL mid-term review or a PLL review*. Further to Reform 2, staff also proposes to streamline the number of Board meetings associated with FCL and PLL *reviews* by offering the possibility of a single Board meeting for the Article IV consultation and FCL or PLL review. Staff would have the option of circulating to the Board a single staff report for the combined Article IV and FCL or PLL review, akin to current practice under other Fund arrangements (though different from other arrangements, reviews for FCL and PLL also focus on the continued qualification of the member for the FCL/PLL).[57] The combined staff report will contain clear and transparent separation between the Article IV surveillance discussions and FCL/PLL-related sections. The FCL/PLL qualification assessment would rely on the Board's assessment of policies in the previous Article IV consultation and staff's appraisal of policies in the "concurrent" Article IV. Following the Board meeting, the Board's assessment of policies under the FCL/PLL (and, in the case of the PLL, assessment of whether the PLL-supported program remains on track) would be reflected in the press release published as part of the document bundle for the combined Article IV Consultation and FCL/PLL review.

[56] In concluding the 2014 Review of the Flexible Credit Line and Precautionary Credit Line, the Executive Board called for concluding Article IV consultations prior to FCL and PLL arrangements' approvals or reviews so as to incorporate the Board's most recent assessment of a member's economic performance in the relevant qualification assessments (BUFF/14/17).

[57] Paragraph 5(a) of the FCL Decision states that a mid-term review "will assess the member's continued adherence to the qualification criteria…", with similar language in the PLL Decision.

B. FCL- and SLL-specific Procedures

50. Staff proposes to simplify the modalities for augmenting access under the FCL and introduce the option of synchronized augmentations. Currently, members requesting an augmentation need to explain the changes in the member's BoP needs and provide justification for the requested increased access. In practice, augmentation requests usually happen at mid-term reviews, when FCL qualification must be reassessed.

- Under this proposal, FCL users would benefit from streamlined augmentation procedures if the augmentation request were made, and considered by the Executive Board, less than six months after the approval of the FCL arrangement or completion of the mid-term review. Streamlined procedures would entail more concise staff reports that, in discussing qualification, can cross-reference the analysis in the previous, most recent, Board document (if applicable), where staff assesses that the qualification still holds. Under the streamlined procedures, the Executive Board would consider and confirm the member's continued qualification and, in such a case, consider the augmentation request. A request for augmentation would normally only require a short staff report providing an updated ESI supportive of increased external risks, as well as developing an adverse scenario to demonstrate increased BoP needs, the case of the higher access, assessment of the member's capacity to repay and a staff assessment that the analysis of the member's qualification as discussed in a previous staff report remains unchanged. The Executive Board confirmation that a member qualifies under the new streamlined procedures for augmentation would not change the date set previously for completion of the mid-term review.
- Additionally, staff proposes extending the process for synchronized FCL requests to FCL augmentations, which would allow the Fund to nimbly respond to instances where a group of FCL users are hit by the same external shock.[58]

51. Staff proposes to include the option of requesting approval of an SLL arrangement through a written communication from the authorities. Currently, after the Board approves an SLL arrangement on a conditional basis, the arrangement only becomes effective once the Fund confirms receipt of the member's signed written communication, including the acceptance of the "offer" and policy commitments.[59] Though the authorities have two weeks to accept the offer from the Fund, given market sensitivities, they are generally likely to want to make the SLL effective as soon as possible, which means that all procedural steps needed to make the SLL effective have to happen within hours of the Board meeting. For members that would prefer an alternative to such

[58] In line with the procedures for synchronized approvals of FCL arrangements, the proposed augmentation of access would be each based on a rigorous assessment of the member's actual or potential balance of payments need and capacity to repay and would take into account the individual and cumulative impact of the access requests of Fund resources. See the Flexible Credit Line Operational Guidance Note, Annex VII, based on Technical Note on Synchronized Approval of Flexible Credit Lines for Multiple Countries; IMF Policy Paper; November 12, 2010.

[59] Such a procedure thus requires a three-step process: the Fund's SLL "offer" to the member, the member's acceptance of the "offer", and the Fund confirming receipt of the acceptance (which in practice, will be a letter from the Managing Director informing the member about the SLL coming into effect. After this is complete, the Board needs to be similarly notified.

procedural steps, the review proposes the option that SLLs, instead of being "offered" by the Board, be requested by the authorities. In such situations, the process would be very similar to FCLs: the authorities would request an SLL arrangement through a written communication that would be attached to the staff report, and the SLL arrangement would become effective upon Board approval of the request. If authorities were to prefer the "offer" process, however, this process would continue to be available.

52. The transition between an SLL arrangement and an FCL arrangement could also be streamlined. If a member opts to transition from an SLL arrangement to an FCL arrangement, and the transition is to be considered by the Board less than 6 months after the SLL arrangement enters effect, an informal Board meeting with a preliminary assessment would not be required. Also, if a member opts to transition between SLL and FCL (in either direction) within the same six months period from the entering into effect/review of the existing arrangement, the staff reports could, in discussing qualification, cross-reference the analysis in the previous, most recent, Board document (if applicable), where staff assesses that the assessment of qualification has not changed, provided that in all cases, the staff report will include an update on the member's BOP problem (which in the case of the transition to an SLL arrangement, will support that the member has the special BOP problem required for SLL qualification). Same as above, under these streamlined procedures, the Executive Board would consider and confirm the member's qualification and, in such case, consider the approval of the new arrangement.

53. Staff also proposes a smoother transition from a stand-alone FCL or SLL arrangement to concurrent use of the FCL and SLL, with no need for an Informal Board in specific circumstances. Should the proposal on inclusion of explicit provisions on concurrent use of the SLL with the FCL be adopted and should a member with an ongoing FCL or SLL arrangement opt to use concurrently the FCL and SLL such that the approval of the new additional arrangement will be considered by the Board less than six months after the stand-alone FCL or SLL arrangement was approved or after the FCL mid-term review was completed, streamlined procedures may apply. Specifically, if the new additional arrangement requested is an FCL arrangement, the informal meeting to conduct the preliminary assessment of qualification would not be necessary. The staff report for the new additional FCL or SLL arrangement to be issued for Board consideration in a case of concurrent use could be more concise in discussing qualification, by cross-referencing the analysis in the previous, most recent, Board document, where staff assesses that the qualification still holds. The staff report will also need to include an assessment confirming that the member has the special BoP problem addressed by the SLL (in case the new arrangement would be an SLL arrangement) or discussing the BoP need of the member (in case the new arrangement would be an FCL arrangement), showing that the combined access under the SLL and the FCL is commensurate to the potential BoP gap in the adverse scenario. The staff report would also include an updated ESI, and the member's capacity to repay. Under the streamlined procedures, the Executive Board would consider and confirm the member's qualification and, in such case, approve the concurrent arrangements.

C. Other Policies

Political Assurances

54. Several recent FCL requests have taken place just prior to elections, with potential changes of government, raising questions about the need for political assurances. Owing to market sensitivities, postponing the approval of a new or successor FCL, SLL, or PLL arrangement request until a new government takes office could be detrimental to a member, given delayed access to FCL/SLL/PLL resources or their temporary discontinuation. The very strong institutional frameworks, as required for FCL or SLL, reduce risks during election periods, as these institutions serve as guardrails that ensure a very strong policy response should an actual BoP need materialize. At the same time, a key requirement of the FCL and SLL (respectively PLL) qualification assessment is that countries remain committed to maintaining very strong (respectively sound) policies and institutional frameworks in the future. Moreover, carving out the FCL, SLL, or PLL from political assurances review would imply that instruments with no or limited ex post conditionality would have weaker political assurances than other GRA instruments. Amid upcoming elections, Colombia's 2022 FCL request and Peru's 2021 review included political assurances from the leading presidential candidates on continuity of key policies and maintaining very strong policy frameworks, considered to provide appropriate safeguards for the proposed arrangements. The FCL and PLL guidance notes suggest first seeking to delink the timing of a request for a new arrangement from the electoral cycle,[60] but this could usually be detrimental to the member as noted above. When it is not possible to delink the arrangement request from the election cycle, the guidance notes stipulate that staff should seek political assurances from electoral candidates that the very strong (or sound policies, in PLL cases) and policy frameworks will be maintained.

55. Staff proposes to reiterate the requirement for political assurances and to consider shorter arrangements to delink approvals from the election cycle where feasible. This review formalizes and reinforces a practice that has been followed in recent cases that—as stated in the FCL and PLL guidance notes—political assurances from main electoral candidates on maintaining very strong (or sound, in the case of PLLs) policies and institutional policy frameworks should be required in the face of upcoming elections. These political assurances represent a forward-looking safeguard for the FCL, SLL, and PLL, as it is often not feasible in practice to delink the timing of an arrangement request or review from the electoral cycle. Further guidance on political assurances will be provided in the forthcoming operational guidance note on conditionality. As part of delinking arrangements, where possible, from the electoral cycle, shorter (one-year, as opposed to two-year) FCL and PLL arrangements could be considered to ensure that the new Fund arrangement would be approved after elections are concluded and there is clarity on the government that will take office, provided that other considerations such as the expected development in external risks are also fully factored in in the choice of the arrangement's duration. Where it is not possible to delink the request in this

[60] For more details, see the FCL operational guidance note, footnote 16.

way, staff should seek assurances from electoral candidates that the very strong policies and policy frameworks will be maintained, in line with the FCL and PLL Guidance Notes.

Safeguards Policy

56. Staff proposes to align the FCL policy with the safeguards policy requirement for a framework between central banks and finance ministries for servicing obligations to the Fund when IMF resources are drawn down for budget financing. Such a framework is typically provided through a Memorandum of Understanding (MoU) between the member's central bank and the government. As part of these arrangements, it is expected that Fund resources will be kept in the government's accounts with the central bank pending their use.[61] Currently, the FCL policy does not include a specific requirement on such an MoU. Discussions on the 2020 Colombia FCL arrangement raised the question of the applicability of this requirement that is otherwise applied for other GRA/PRGT arrangements that have IMF resources directed toward budget support.[62] In this light, staff proposes to modify the FCL policy by requiring central banks and finance ministries to agree on a framework clarifying responsibilities for timely service of obligations to the Fund when FCL resources are expected to be drawn for budget financing, including that Fund disbursements will be deposited in the government's accounts at the central bank pending their use.

SLL Safeguards Requirements

57. Staff proposes clarifying safeguards requirements for SLL staff reports. Relatively low access and short maturity mean that an SLL arrangement is unlikely to have a significant bearing on medium-term sustainability or on multi-year macroeconomic projections (as the instrument would primarily serve as a liquidity management resource). For that reason, staff proposes not requiring standalone SLL staff reports to feature a full-fledged adverse scenario. Similarly, given that the SLL is mainly a liquidity instrument with a relatively low access level and a repurchase period of only 12 months, the capacity to repay analysis can be streamlined, focusing on short-term liquidity risks.

FINANCIAL CONSIDERATIONS

To ensure the Fund's continued sound management of its precautionary toolkit, this section reviews a key safeguard in case of a significant rise in demand for precautionary facilities, and revisits consideration—but does not propose changes—relating to time-based commitment fees and the scoring of the Forward Commitment Capacity (FCC).

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[61] See 2010 and 2015 Safeguards Policy reviews (BUFF/10/15, SM/10/178 and SM/15/250).

[62] In practice, the Colombian authorities agreed that such an MoU is desirable and implemented it.

A. Review Clause

58. The review proposes to add the SLL to the review clause.

- The current long-standing "review clause" would trigger a new review of the precautionary toolkit whenever aggregate outstanding credit and commitments under the FCL and PLL instruments reach SDR 150 billion (Decision No. 16286).
- When introduced in April 2020 in the context of the Fund's COVID-19 response, the SLL was not at that time included in the review clause, owing to the increased Board monitoring of Fund resources in the pandemic environment and to avoid preempting the current review of precautionary instruments.
- As proposals for this review could be conducive to higher lending under the SLL, including under concurrent use with the FCL and higher access limits, it would be appropriate to include SLL commitments towards the trigger for a review going forward.

59. The threshold amount for the review clause will remain unchanged. As of June 30, 2023, the Fund's current outstanding credit and commitments under the FCL, PLL, and SLL total SDR 70.9 billion.[63] The current review clause threshold of SDR 150 billion would be approached only in the event of a doubling of lending under these instruments. In staff's view, this threshold remains an important safeguard while preserving room for higher demand for precautionary-basis financing. Accordingly, the review will stipulate that the FCL, SLL, and PLL will be reviewed whenever aggregate outstanding credit and commitments under these instruments reach SDR 150 billion or following the time-based reviews in 2025 for the SLL and every 5 years thereafter.

B. Time-Based Commitment Fee

60. In recent years, a number of Directors have called for strengthening exit incentives from prolonged use of Fund's precautionary facilities at high access levels. The 2017 review of precautionary facilities explored—but did not adopt—time-based commitment fees (TBCFs) as an option for strengthening incentives to exit precautionary arrangements. This review revisits design issues for possible TBCFs in light of more recent experiences with precautionary arrangements (Annex VIII). The review also explores reducing the level of the commitment fee charged at lower access levels to encourage additional qualifying members to seek precautionary support from the Fund.[64]

61. A TBCF would subject an arrangement to an additional commitment fee once the level of undrawn credit, including under previous arrangements, has remained above a specified

[63] This comprises SDR 65.5 billion in undrawn credit and SDR 5.3 billion in credit outstanding under the FCL and PLL. No credit or commitments are currently outstanding under the SLL.

[64] In line with the principle of uniformity set out in Article V, Section 8(d), such a reduction in the level of commitment fees would apply to all GRA arrangements.

access threshold for a defined period. The TBCF would be triggered based on the member's use of previous precautionary arrangements. More specifically, the TBCF would be triggered if the member had received access to the Fund's GRA resources above a certain level over a period of time but, within this period, had not made a purchase. It would be irrelevant if this period was under one or more arrangement, including expired arrangements. Arrangements would remain subject to the fee until the level of undrawn credit fell below the relevant threshold, through purchases, reduction of access, or upon expiration of the arrangement. The 2017 Review explored increasing the commitment fee rate by 10–20 basis points for members with precautionary arrangements above 575 percent of quota after 48 months. This review explores the option of triggering the higher commitment fee after 24 months.

62. The review does not propose to introduce a TBCF. Applying the parameters from the 2017 Review, no current users of precautionary arrangements would incur additional fee in the immediate future, given that all prolonged users have access levels below the hypothetical threshold considered. Hence, such a TBCF would have a limited impact on incentivizing exit in the immediate future. Introducing a tighter TBCF at the current juncture of elevated global vulnerabilities would weaken the responsiveness of the Fund's toolkit to membership's needs by making exit time- rather than state-dependent. Moreover, owing to the legal requirement of uniformity of charges, the application would not be restricted to arrangements that are treated as precautionary, thus potentially having unintended implications for large drawing arrangements that go off track.

63. The review does not propose reducing the commitment fee for low-access arrangements to encourage use by additional qualifying members. Such policy would have a negative impact on Fund income, imposing costs without necessarily the benefit of a strong increase in the number of additional members seeking precautionary support (see Annex VIII for illustrative calculations).

C. Scoring of Commitments on a Precautionary Basis in the Fund's Liquidity Measure

64. A few Directors have asked staff to reconsider the possibility of moving from the current practice of counting precautionary arrangements at full value in the calculation of Fund liquidity.[65] The Fund's definition of the GRA's liquidity, the Forward Commitment Capacity (FCC), currently reflects the full amount of all commitments of GRA resources, whether approved on a disbursing or a precautionary basis. A few Directors have requested consideration of a "partial scoring" regime that would recognize a lower probability of actual drawings under arrangements approved on a precautionary basis. Partial scoring would treat only part of the amounts under precautionary arrangements as committed usable resources. This is perceived to enable the Fund to commit more resources on a precautionary basis for a given level of Fund resources.

[65] Partial scoring was already discussed in the 2017 Review of Precautionary Arrangements, and ultimately rejected then by the Executive Board.

65. However, staff does not support moving from full to partial scoring of precautionary facilities, which could expose the Fund to significant liquidity risks—and delay and complicate potential activation of the Fund's borrowed resources. Partial scoring would not create any additional resources for Fund financing, while increasing the risk that the Fund's financing commitments would exceed its available resources. As discussed in detail in Annex:

- Calls for partial scoring of precautionary arrangements, motivated by the uncertainty of possible drawings, implicitly assume that members' drawings would be uncorrelated. However, to the extent that drawings are triggered by systemic events—such as a tightening in global financial conditions—drawings could well be correlated. Should Fund commitments thus exceed available resources, the Fund could potentially be in a position of not being able to meet its financial commitments, undermining the Fund's credibility, and potentially negating the value of precautionary arrangements. In staff's view, this is incompatible with the Fund's role as a global crisis lender.

- If there is any doubt in the Fund's ability to honor its financing commitments in a crisis situation, individual borrowers with precautionary arrangements could face perverse incentives to draw down their arrangements ahead of other borrowers, raising the possibility of a "run" on the Fund's usable resources.

- Moreover, the Fund's borrowed resources can be used to finance only those lending commitments that are made during a period when borrowed resources are activated. Commitments approved outside of an activation period must be financed exclusively from quota resources, which could become depleted.

- Moving to an FCC based on partial scoring would delay activation of borrowed resources and elevate the Fund's liquidity risks. Full scoring is embedded in the current FCC definition[66] which refers to "undrawn balances under existing arrangements" as a factor which decreases the FCC level. Applying partial scoring of these undrawn balances to the FCC would result in a higher FCC level compared with full scoring. As Fund borrowing cannot be activated unless the FCC is projected to drop below certain levels, a higher FCC level due to partial scoring would thus delay such activation and increase the risk that the Fund might not be able to honor lending commitments if they exceed the Fund's available resources.[67]

- Moreover, as both the decision on the New Arrangements to Borrow (NAB Decision) and the 2020 Bilateral Borrowing Agreements (2020 BBAs) include clauses referencing the FCC as defined under the current FCC Decision, any modifications to the FCC definition would raise the

[66] The FCC definition is set out in Decision No. 14906-(11/38) (the "FCC decision"; adopted April 20, 2011).

[67] In view of existing U.S. legislation, the Managing Director will not generally propose an activation of the NAB unless the FCC, excluding borrowing resources, is expected to drop below SDR 100 billion. The 2020 Borrowing Agreements provide that the Fund may not activate these resources unless the FCC, taking into account all available uncommitted NAB resources, falls below SDR 100 billion.

question of the need for potential changes to the NAB Decision and 2020 BBAs, and in this regard the consent of NAB participants and 2020 BBA creditors.

ENTERPRISE RISKS

66. This section discusses enterprise risks considerations related to the following reforms proposed by staff:

- removal of exit expectations for low-access precautionary FCL arrangements;
- explicit provisions enabling concurrent use of the SLL with the FCL;
- increases in PLL limits and caps, and SLL access limit; and
- modification of the EA PLL DSA requirements.

Risk to the Fund <u>Without</u> these Proposed Reforms:

Business risks. Not proceeding with reforms to the precautionary toolkit would weaken the Fund's response to the membership's evolving needs and could lead to under-provision of Fund financing against shocks for members with very strong or sound economic fundamentals and institutional policy frameworks.

Strategic risks. An inadequate Fund response to members' needs could lead to some members' unduly increased reliance on self-insurance and other sources of financing such as BSLs or RFAs, leading to a more fragmented and less efficient GFSN. It may also result in an expensive accumulation of reserves by member countries, which could also contribute to larger global imbalances and slower economic growth.

Reputational risks. The Fund could be perceived as lacking alignment with its members' needs, potentially eroding trust in the institution's effectiveness and members' willingness to engage.

Risk to the Fund <u>With</u> these Proposed Reforms:

Credit risks. With an increase in PLL and SLL limits and allowing for no-exit expectations for low-access precautionary FCL arrangements and explicitly permitting concurrent FCL/SLL use, credit risk to the Fund could potentially rise compared to the status quo. These risks, however, are mitigated by several factors:

- The continued application of the qualification criteria for the FCL, SLL, and PLL, which require very strong (FCL/SLL) or sound (PLL) economic fundamentals and institutional policy frameworks;

- For PLL arrangements, access limits would remain anchored to the GRA EA thresholds;

- For FCL arrangements, the expectation that members with access exceeding 200 percent of quota would gradually reduce access or exit would be maintained; and

- Standard safeguards for access to Fund resources, including assessments of debt sustainability and CtR, would continue to apply.

Any implications for the targeted financial protection against the risk of non-payment would be considered in a holistic manner at the time of the next precautionary balances review. Under the current framework for assessing the adequacy of precautionary balances, commitments of precautionary arrangements are not included in the calculation of the forward-looking credit measure that determines the indicative range for the precautionary balances coverage ratio, but they are taken into account judgmentally when setting the precautionary balances target.

The proposed modification to the PLL debt sustainability requirements would not materially impact the quality or accuracy of staff's assessment. Hence, it is not expected to increase credit risk significantly.

Liquidity risks. The increase in PLL and SLL access limits, the concurrent use of FCL and SLL, and no-exit expectations for low-access precautionary FCL arrangements could potentially lead to significantly higher demand for precautionary lending, which would reduce the Fund's liquidity and commit a high share of lending capacity. In the event of especially high demand, this could also give rise to the need to activate the Fund's borrowed resources—though in the baseline, any proposal to activate borrowed resources would depend on developments in demand for non-precautionary Fund lending as well. Liquidity-related risks are somewhat mitigated by the review clause, which requires a new Review of Precautionary Arrangements if precautionary credit and commitments reach SDR 150 billion (from the current SDR 72 billion), as well as by the same factors mitigating credit risk.

Business risks. If higher take-ups of FCL, SLL, and PLL arrangements were perceived as reflecting a loosening in lending standards, members could assume that they would be able to qualify for such arrangements with weaker policies. In that case, the Fund's policy advice could lose traction. This risk is mitigated by qualification requirements at the time of approval of an FCL/PLL/SLL arrangement and subsequent review(s).

Operational risk. The concurrent use of FCL and SLL instruments, with different repurchase periods, could be operationally challenging. This risk is mitigated by the Fund's deep experience with multiple and elaborated operational procedures.

Staffing constraint risk. Should the proposed changes to the precautionary facilities result in significant increase in demand or these facilities, this would also result in higher staffing needs both in the area and functional departments. This would require reprioritization of other workstreams in the environment of Fund's real flat budget.

67. Staff also considered, but did not propose, other reforms. These included most notably:

(i) a shift to partial scoring whereby only part of the amounts under precautionary arrangements would be treated as committed usable resources—which would create significant liquidity risk by delaying and complicating activation of borrowed resources; and

(ii) a reduction in commitment fees to incentivize the use of precautionary instruments, which would generate income risks by reducing lending income.

ISSUES FOR DISCUSSION

68. Staff would particularly welcome Board views and comments on the following questions:

- Do Directors agree that precautionary arrangements have served the membership well during the pandemic and since the start of war in Ukraine? Do Directors agree that there is a need to refine these instruments to ensure that precautionary arrangements are fit for purpose in the current context of heightened global risks?
- Do Directors concur with clarifications of the qualification assessment and process on AML/CFT, governance issues, political assurances, and safeguards?
- Do Directors agree with the proposed refinement on debt sustainability for the EA PLLs (¶23)?
- Do Directors agree that exit out of high-access FCLs should be state-dependent and encouraged only when access exceeds 200 percent of quota?
- Do Directors agree with the possible increase of the annual access limit at approval of the PLL, and of the PLL instrument caps as discussed above (¶46)?
- Would Directors favor explicit provisions on concurrent use of the SLL with the FCL and increasing the SLL access limit as discussed above (¶s 39-43)?
- Do Directors concur with the options proposed to streamline the number of Board meetings associated with the approval and review of FCL, SLL and PLL arrangements?
- Do Directors favor simplifying the transition from an SLL to an FCL, and vice versa, streamlining the FCL augmentation process, and extending simplified procedures for transitioning from a stand-alone FCL or SLL to concurrent use?
- Do Directors concur with staff recommendations not to introduce changes to commitment fees or to scoring of precautionary arrangements?
- Do Directors agree with the need to develop an outreach plan to increase awareness about precautionary arrangements, and the possibility of synchronized SLLs or FCLs?

Annex I. Overview of FCL, SLL, PLL and Precautionary SBA Arrangements Approved in 2018–23

Country	Year	Facility	Access			
			Percent of GDP at approval	Percent of Quota at approval	Amount at approval (SDR million)	Amount Drawn (SDR million)
Armenia	2019	SBA	1.8	140	180	309
	2022	SBA	1.0	100	129	0
Chile	2020	FCL	9.9	1,000	17,443	0
	2022	SLL	1.0	145	2,529	0
	2022	FCL	6.0	800	13,954	0
Colombia	2018	FCL	3.3	384	7,848	0
	2020	FCL	6.5	600	12,267	3,750
	2022	FCL	3.1	350	7,156	0
Georgia	2022	SBA	1.5	100	210	0
Honduras	2019	SBA	0.8	60	150	281
Jamaica	2023	PLL	5.6	190	728	0
Kosovo	2023	SBA	1.0	97	80	0
Mexico	2019	FCL	4.9	500	44,564	0
	2021	FCL	4.0	400	35,651	0
Morocco	2018	PLL	2.5	240	2,151	2,151
	2023	FCL	3.6	417	3,726	0
North Macedonia	2022	PLL	4.0	290	407	84
Panama	2021	PLL	4.4	500	1,884	0
Peru	2020	FCL	5.6	600	8,007	0
	2022	FCL	2.4	300	4,004	0
Serbia	2022	SBA	4.2	290	1,899	786

Notes:
Data as of May 2023.
Access under Armenia's 2019 SBA was augmented to SDR 308.8 million (239.8 percent of quota) in May 2020.
Access under Honduras' 2019 SBA was augmented to SDR 258.1 million (103.3 percent of quota) in June 2020, and again to SDR 358 million (143.3 percent of quota) in September 2021.
Serbia and North Macedonia intend to treat their respective arrangements (SBA and PLL) on a precautionary basis during the second year of the program.

Annex II. Fund Precautionary Arrangements and Associated Features

	Nature of BoP needs	BoP shock	Access (% quota)	Ex-ante Qualification	Ex-post conditionality	EA policy	Duration	Exit expectations
FCL	Potential/ Actual	Any shocks	No limit*	**Very strong** policy and institutions	No	No	1 or 2 years	Yes
SLL	Potential	Short-term, moderate, repeated needs from capital flow volatility	145	*Same as FCL*	No	No	1 year	**No**
PLL	Potential/ Actual	Any shocks	500* (250/yr)	**Sound** fundamentals and inst. frameworks	Key weak areas (PA/PC/IT/SB)	Yes	6 months, 1 or 2 years	Yes
Prec. SBA	Potential	Potential (for prec. use)	No limit*	N/A	Critical areas (PA/PC/IT/SB)	Yes	6–36 months	Yes

** Actual access is informed by BoP gap in adverse scenario*

	Commitment fees	Lending rates	Service Charges	Repurchase period
FCL **PLL** **Prec. SBA**	**Refundable upon disbursement** 15 bps up to 115% quota, then 30 bps up to 575% quota, then 60 bps above 575% quota	Normal charges; **Time and level**-based surcharges	Normal service charge 50 bps	3¼–5 years in eight equal quarterly installments
SLL	**Non-refundable** 8 bps	Normal charges; **Level**-based surcharges	21 bps	12 months

Annex III. Timing of Article IV Consultations for FCL and PLL Arrangements Approved Since 2017

	Year of FCL/PLL approval	Date of preceding AIV Board	Date of FCL/PLL approval	# of days between AIV Board and FCL/PLL Formal Board
		FCLs		
Mexico	2017	13-Nov-17	30-Nov-17	17 days
	2019	05-Nov-19	25-Nov-19	20 days
	2021	05-Nov-21	19-Nov-21	14 days
Colombia	2016	20-May-16	13-Jun-16	14 days
	2018	30-Apr-18	25-May-18	25 days
	2020	17-Apr-20	01-May-20	14 days
	2022	04-Apr-22	29-Apr-22	25 days
Morocco	2023	24-Jan-23	03-Apr-23	2 months and 2 days
Poland	2017	05-Jul-16	13-Jan-17	6 months and 8 days
Chile	2020	09-Nov-18	29-May-20	1 year, 6 months and 20 days
	2022	23-Apr-21	20-May-22	1 year and 27 days
Peru	2020	14-Jan-20	28-May-20	4 months and 14 days
	2022	02-May-22	27-May-22	25 days
Average (when less than 1 month)				*19 days*
		PLLs		
Morocco	2018	12-Mar-18	17-Dec-18	9 months and 5 days
Panama	2021	26-Mar-20	20-Jan-21	9 months and 25 days
North Macedonia	2022	16-Feb-22	22-Nov-22	9 months and 6 days
Jamaica	2023	10-Feb-23	02-Mar-23	20 days
Average (when less than 1 month)				*20 days*

Annex IV. Precautionary SBA Case Studies

A. Armenia – 2019 Precautionary SBA

Background. Armenia has had a series of Fund arrangements since the GFC: an SBA in 2009, an ECF/EFF in 2010, and an EFF in 2014. Despite good macroeconomic progress through these arrangements, public debt remained elevated in 2019, and the economy was still vulnerable to external shocks, with growth capacity constrained by structural issues linked to business climate and corruption. As such, the government requested a 140 percent of quota SBA in May 2019, followed by the current 2022 SBA.

Objectives and Design. The 2019 SBA aimed to maintain macro stability through strong policies and structural reforms to generate higher, more inclusive, and resilient growth. As such, the program aimed at promoting growth-friendly fiscal consolidation, further strengthening the monetary policy framework and maintaining a flexible exchange rate system, safeguarding the financial system and improving access to finance, and implementing strong structural reforms. To do so, the program had four Quantitative Performance Criteria (QPCs), a Monetary Policy Consultation Clause (MPCC), four Indicative Targets (ITs), and 32 Structural Benchmarks (SBs) across 6 reviews.

Duration, Access, and Disbursements. In 2019, an SBA was approved for 3 years, 140 percent of quota, and initially intended to be precautionary. In 2020, the authorities successfully requested an augmentation of 100 percent of quota (SDR129 million) to cover the BoP needs related to the pandemic and reflecting the tightening of global financial conditions. They drew fully on the first three tranches available to address emergency external and budgetary needs, followed by full drawing of the remaining tranches upon completion of the later reviews.

Performance. Performance under the 2019 SBA was sound. The first three reviews were completed with minor delays and all QPCs were met, though the lower bound of the MPCC was breached in the second review. QPCs and ITs for the combined fourth and fifth[1] review were met except for the Net International Reserve (NIR) floor and the breach in the upper-bound of the MPCC. The sixth review was completed successfully in April 2022 and all QPCs, ITs, and MPCC were met. Implementation of the structural reform agenda was mixed: two out of four SBs for the sixth review were not met.

Impact. The arrangement, along with support from other International Financial Institutions (IFIs), helped mitigate adverse effects of the regional conflict and ease BoP pressures during the COVID crisis, without use of Fund emergency financing. More broadly, the 2019 SBA had served Armenia well and many of the program objectives had been achieved, including implementation of appropriate fiscal policies to ensure targeted health and social spending while preserving fiscal sustainability, increased reserve coverage, structural reforms improving transparency, governance, business environment, and social spending adequacy. The Armenian economy remained vulnerable to external shocks in 2022 (spillovers from the war in Ukraine, global financial tightening, and a slowdown in major trading partners) and still faced structural challenges, including high structural

[1] The announcement of the June 2021 snap elections delayed the fourth review.

unemployment and low productivity growth, which led to the request of another precautionary SBA in December, for 100 percent of quota (SDR129 million).

B. Georgia – 2022 Precautionary SBA

Background. Georgia benefitted from three consecutive SBAs with decreasing access levels between 2008 and 2017, one of which was an SBA-SCF used on a precautionary basis (and not drawn down). The 2017-21 EFF was implemented successfully, with all reviews completed and an extension and augmentation approved during the pandemic. Seeking to build on the success of the EFF by pursuing their reform agenda, and being familiar with the SBA instrument, the authorities requested a precautionary SBA in 2022, for the same access level as the 2017-21 EFF at approval (100 percent of quota).

Objectives and Design. Recognizing significant near-term risks to the external environment, the authorities stated their intent to treat the program as precautionary to send a strong signal of their commitment to credible policies and macroeconomic stability. The main program objectives comprise medium-term fiscal adjustment to restore fiscal buffers, strengthening public financial management and revenue generation to limit fiscal risks and create room, for priority spending, maintaining a sufficiently tight monetary stance to bring inflation to target, bolstering financial sector resilience, and implementing structural reforms to strengthen labor market participation and inclusive growth. The program is being monitored through an inflation consultation clause (ICC), fiscal, debt- and reserve-related QPCs, current primary spending and general government domestic expenditure arrears ITs and SBs focused on controlling fiscal risks, improving tax policy and administration, and following up on 2021 FSAP recommendations.

Duration, Access, and Disbursements. The precautionary SBA was approved for a duration of three years, with access evenly phased across 6 reviews. The total access level would help address the potential BoP gap that would likely open in case of a protracted downside shock such as due to an escalation and prolongation of the war in Ukraine (via higher commodity prices, lower exports, and weaker tourism revenue and financial inflows). As of May 2023, Georgia had not drawn on the SBA.

Performance. At the time of this review, one review has been successfully completed under the ongoing precautionary SBA in December 2022, with all QPCs being met, end-June 2022 inflation within the inner bands of the ICC, four SBs met and four implemented as PAs before the First Review. Staff level agreement has been reached on May 11, 2023, for the Second Review.

Impact. While it is early to assess whether objectives of the current SBA will be met or not, Georgia's successful experience with its previous programs, including the precautionary SBA-SCF from 2012-14, encouraged it to request an additional precautionary SBA in 2022, to provide a strong anchor for macro policies and a signal of policy credibility to donors and foreign investors. While net external loan inflows had decreased post-Covid, general government loans (from private and public sources), supported by the program, were still expected at program approval to hover around pre-pandemic levels in the following years.

C. Honduras – 2019 Precautionary SBA

Background. Honduras's two-year SBA/SCF was approved in July 2019 for precautionary use, with combined access of 90 percent of quota (SDR 224.8 million or about USD 311 million), commensurate with the BoP needs that could arise from a negative terms-of-trade shock. It succeeded a series of three precautionary SBA arrangements since 2008, of which the last two were also blended with the SCF. Under the preceding SBA/SCF which spanned 2014–17, Honduras made great strides in reducing macroeconomic imbalances and strengthening its policy frameworks. As a result, confidence improved, and debt spreads declined steadily and translated into better financing terms for private and public investment. Nevertheless, challenges remained to reduce vulnerabilities and risks, including high levels of poverty and informality, governance weaknesses, and the deteriorating financial situation of the public electricity utility.

Objectives and Design. The 2019 SBA/SCF was requested to support reforms aimed at ensuring fiscal and debt sustainability while protecting investment and social spending; modernizing the monetary and financial policy frameworks to buffer shocks and maintain stability; and improving governance and the business climate. At inception, the 5-review SBA/SCF was predicated on 7 quantitative performance criteria (QPCs), 5 indicative targets (ITs), and 13 structural benchmarks (SBs) on fiscal, monetary, and debt issues. Three prior actions in the electricity sector were also included. New SBs were introduced throughout the program period to sustain reforms in fiscal governance, the anti-corruption, monetary, and financial frameworks, and the electricity sector.

Duration, Access, and Disbursements. The SBA/SCF was treated as precautionary up until the authorities drew on SDR 104.92 million (42 percent of quota) in Fund resources in late March 2020 to respond to the pandemic. Total access was subsequently augmented to 155 percent of quota (SDR 387.2 million or about USD 531 million) at the second review and to 215 percent of quota (SDR 537.1 million or about USD 773 million) at the fourth review to continue supporting the authorities' pandemic response and help finance reconstruction efforts following the two tropical storms that struck Honduras in November 2020, damaging infrastructure and crops, and halting manufacturing. The program was also extended by four months at the third review and by an additional two months at the fourth review to help maintain the reform momentum amid an increasingly uncertain outlook.

Performance. Performance under the SBA/SCF was broadly satisfactory, with the first four reviews completed in time, despite the COVID-19 pandemic and the end-2020 tropical storms which caused the non-observance of some program targets. For instance, the end-December 2020 QPC on the fiscal balance was missed owing to higher-than-expected pandemic and storm-related emergency spending, the public electricity utility accumulated arrears from end-June 2020 due to mounting liquidity pressures, while the IT on social spending was breached both at end-December 2020 and end-June 2021 following a shift of resources to storm-related spending. Some SBs were also temporarily delayed. As a result, program targets were recalibrated to accommodate the fiscal policy response, including higher expenditure from reconstruction needs and continued emergency measures. The SBA/SCF expired in January 2022, without the completion of the fifth and final review, due to the weakening of the anti-money laundering legislation.

Impact. The SBA/SCF was a critical anchor for macroeconomic policies and reforms, supporting important progress in improving revenue administration, strengthening public financial management, and enhancing expenditure transparency. While the pandemic and tropical storms slowed implementation, the SBA/SCF provided enough flexibility to manage these large shocks within the medium-term framework, initially through rapid access to Fund resources at the onset of the COVID-19 crisis thanks to the purchase rights accumulated since program approval. Target recalibrations, program extensions, as well as access augmentations and rephasing also showcased the flexibility of the SBA and SCF in catering to members' needs in difficult times. Relatedly, the SBA/SCF helped Honduras catalyze financing from multilateral and bilateral donors, and tap international markets, as evidenced by the successful USD 600 million sovereign bond placement in June 2020.

D. Serbia – 2022 Hybrid SBA

Background. Following a disbursing SBA during the GFC, a successor *precautionary* SBA was approved in 2011 to insure against external risks and provide a policy anchor. However, the program went off track quickly due to fiscal slippages related to re-election spending and expired before the first review. A new *precautionary* SBA with same level of access was requested in 2015 to restore public debt sustainability, enhance financial sector resilience, and improve competitiveness and medium-term growth potential. Significant progress was made during this SBA, which remained undrawn, such that the authorities requested a Policy Coordination Instrument (PCI) in 2018 and a successor one in 2021. Serbia's economy rebounded quickly from the Covid pandemic, and buffers were rebuilt through appropriate consolidation. However, with more challenging external conditions, Serbia's economic outlook weakened despite its still strong macro policies, which led the authorities to shift from the on-track PCI to a hybrid SBA in end-2022.

Objectives and Design. The 2022 SBA builds on the 2021 PCI agenda, maintaining macro stability, strengthening fiscal frameworks, advancing structural reforms for more inclusive and sustainable growth, and addressing Serbia's external, fiscal financing needs, and energy crisis, and increasing buffers. At program approval, the 2 year/4 review SBA includes three QPCs, one IT, one continuous performance criterion, an inflation consultation band, three PAs, and nine SBs. Key policies under the SBA include: (i) energy policies to restore energy SOEs' financial viability and laying foundations for a green transition; (ii) tight monetary and fiscal policies to help manage the external and fiscal financing needs, control inflation, and support the stabilized exchange rate; and (iii) structural reforms to strengthen SOE governance and oversight.

Duration, Access, and Disbursements. An access level of SDR1,899 million (290 percent of quota) was approved under the 2022 SBA, with the first part covering actual BoP needs (in three purchases), and the second part to be treated as precautionary. An adverse scenario that assumes an intensification of the ongoing shocks arising from the war in Ukraine illustrates a full drawing on the precautionary part of the SBA in 2024 to help boost up reserves under increased financing need to 97.6 percent of the ARA metric in 2024.

Performance. The first review under the 2022 SBA is scheduled to be completed in June 2023.

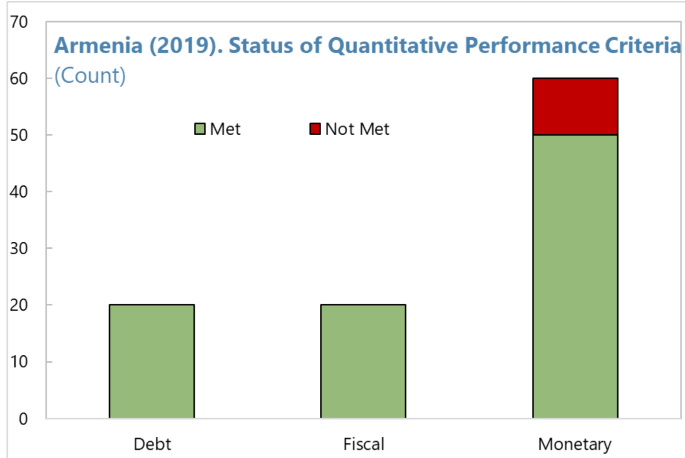
Annex IV Table 1. Users of Precautionary SBA Arrangements: Overview of Facilities Since the Global Financial Crisis

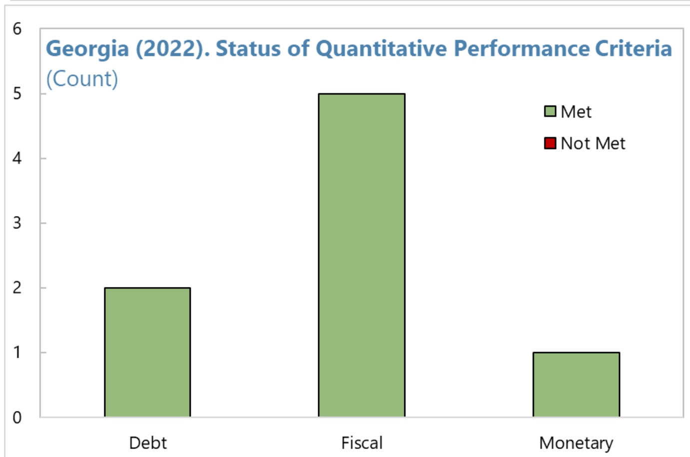
Country	Year	Facility	Duration (months)	Percent of Quota at approval	Amount at approval (SDR million)	Quota at approval (SDR million)	Intended use at approval
Armenia	2008	ECF	4	10	9.2	92	Disbursing
	2009	SBA	16	400	368.0	92	Disbursing
	2010	ECF-EFF	36	290	266.8	92	Disbursing
	2014	EFF	40	89.4	82.2	92	Disbursing
	2019	SBA	36	139.8	180.0	129	Precautionary
	2022	SBA	36	100	128.8	129	Precautionary
Georgia	2008	SBA	33	317	477.1	150	Disbursing
	2012	SBA-SCF	24	166	250.0	150	Precautionary
	2014	SBA	32	67	100.0	150	Disbursing
	2017	EFF	48	100	210.4	210	Disbursing
	2022	SBA	36	100	210.4	210	Precautionary
Honduras	2008	SBA	12	30	38.9	130	Precautionary
	2010	SBA-SCF	18	100	129.5	130	Precautionary
	2014	SBA-SCF	36 and 24	100	129.5	130	Precautionary
	2019	SBA-SCF	30	90	224.8	250	Precautionary
Kosovo	2023	SBA	24	97	80.1	83	Precautionary
Serbia	2009	SBA	27	75	350.8	468	Disbursing
	2011	SBA	18	200	935.4	468	Precautionary
	2015	SBA	36	200	935.4	468	Precautionary
	2022	SBA	24	290	1898.9	655	Disbursing

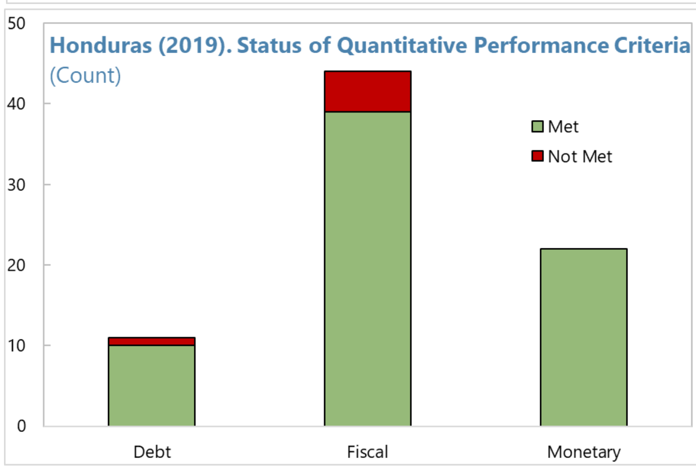
Source: FIN database and IMF staff calculations.

Note: Armenia (2022), Georgia (2022), Serbia (2022) ongoing. Actual duration including extensions, expected duration for ongoing arrangements. Honduras was approved a 36-month SBA and 24-month SCF in 2014 under a blended arrangement. Serbia's 2022 SBA disbursing (precautionary) the first (second) year of the program. Serbia was approved a policy coordination instrument (PCI) in 2018 and 2021.

Annex IV Figure 1. Performance under Precautionary SBA Arrangements since 2017: Status of Quantitative Performance Criteria as of the Last Review



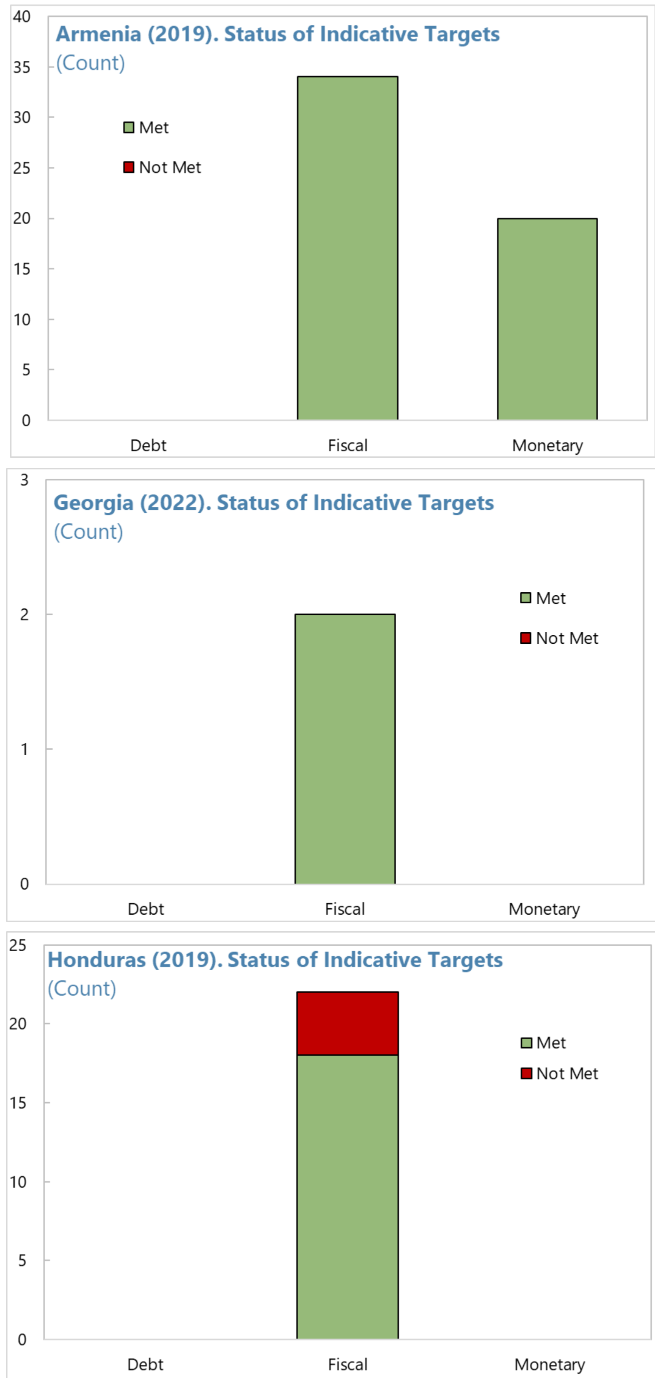




Source: MONA and IMF staff calculations.

Note: For Armenia, status as of the 6th review under the 2019 SBA. For Georgia, status as of the 1st review of the 2022 SBA. For Honduras, status as of the 4th review under the 2019 blended SBA/SCF.

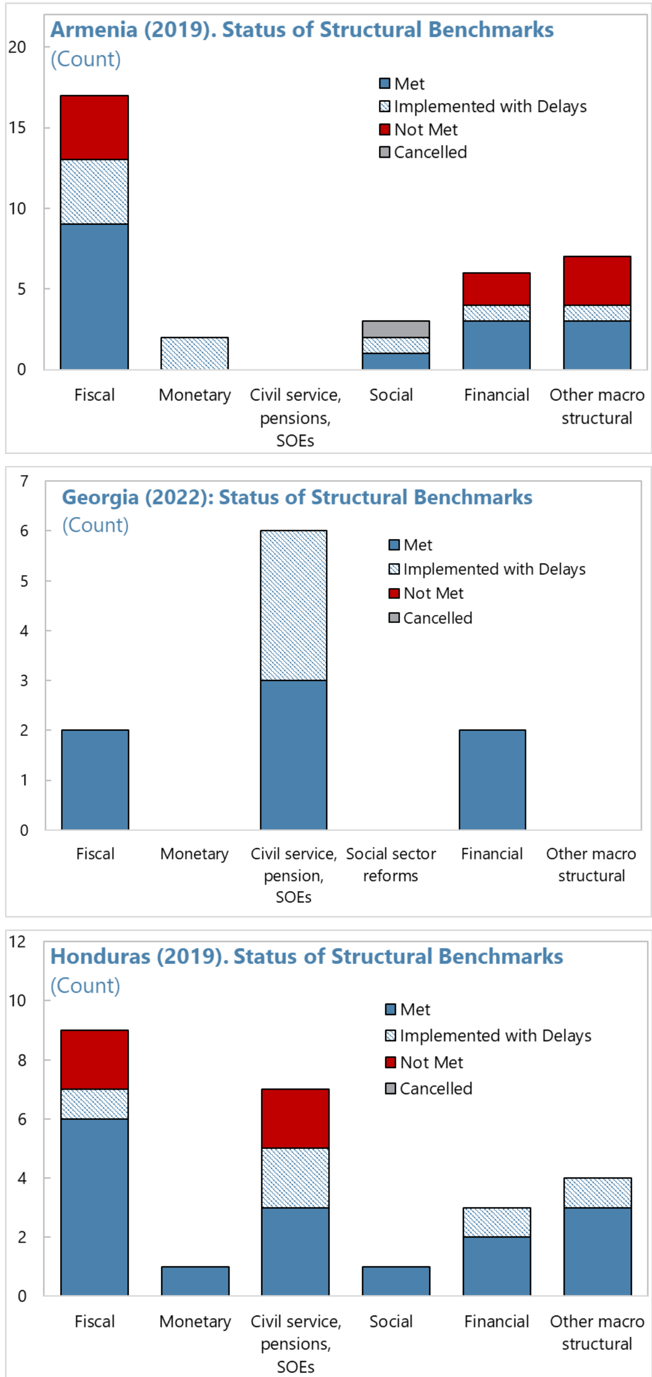
Annex IV Figure 2. Performance under Precautionary SBA Arrangements since 2017: Status of Indicative Targets as of the Last Review



Source: MONA and IMF staff calculations.

Note: For Armenia, status as of the 6th review under the 2019 SBA. For Georgia, status as of the 1st review of the 2022 SBA. For Honduras, status as of the 4th review under the 2019 blended SBA/SCF.

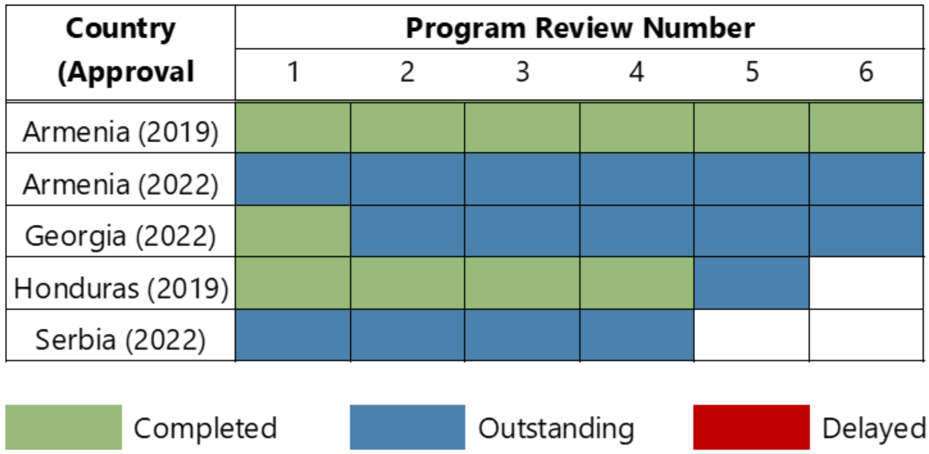
Annex IV Figure 3. Performance under Precautionary SBA Arrangements since 2017: Status of Structural Benchmarks as of the Latest Review



Source: MONA and IMF staff calculations.

Note: For Armenia, status as of the 6th review under the 2019 SBA. For Georgia, status as of the 1st review of the 2022 SBA. For Honduras, status as of the 4th review under the 2019 blended SBA/SCF.

Annex IV Table 2. Performance under Precautionary SBA Arrangements since 2017: Status of Reviews



Source: MONA and IMF staff calculations.

Note: For Honduras, the blended SBA/SCF expired without completing the fifth and last review.

Annex V. FCL/SLL/PLL Qualification Assessments, 2018-22

1. FCL and SLL Arrangements

	Chile 2020 FCL	Chile 2022 SLL	Chile 2022 FCL	Colombia 2018 FCL	Colombia 2020 FCL	Colombia 2022 FCL	Mexico 2019 FCL	Mexico 2021 FCL	Peru 2020 FCL	Peru 2022 FCL	Morocco 2023 FCL
1. *A sustainable external position* (EBA assessment at least "moderately weaker")	broadly in line	moderately stronger	moderately stronger	moderately weaker	moderately weaker	moderately weaker	broadly in line	stronger	broadly in line	broadly in line	broadly in line
2. *A capital account dominated by private flows* (share of private flows in capital flows>50 percent)	82 percent	74 percent	75 percent	75 percent	79 percent	76 percent	80 percent	83 percent	76 percent	80 percent	52 percent
3. *A track record of steady sovereign access to sovereign markets at favorable terms* (issued in at least 3 of the last 5 years in the cumulative amount of at least 50 percent of the quota)	issued debt in each of the last 5 years in the amount of 515 percent of the quota	issued debt in each of the last 5 years in the amount of 1,500 percent of the quota	issued debt in each of the last 5 years in the amount of 1,500 percent of the quota	issued debt in each of the last 5 years in the amount of 450 percent of the quota	issued debt in each of the last 5 years in the amount of 480 percent of the quota	issued debt in each of the last 5 years in the amount of 686 percent of the quota	issued debt in each of the last 5 years in the amount of 1,600 percent of the quota	900 percent of quota	issued debt in 3 of the last 5 years in the amount of 330 percent of the quota	issued debt in 4 of the last 5 years	issued debt in 4 of the last 5 years for a cumulative amount of US $9 billion (more than 7 times Morocco's quota)
4. *A comfortable reserve position* (reserves> 100 percent of ARA metric)	90 percent	91 percent	82 percent	146 percent	142 percent	139 percent	120 percent	127 percent	255 percent	280 percent	133 percent
5. *Sound public finance* (debt sustainable with HP)	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability
6. *Low and stable inflation* *(inflation in single-digits in the last 5 years, shown: average inflation in the 3 years preceding qualification)*	3 percent	3 percent	3.8 percent	5.6 percent	3.7 percent	3.2 percent	5.0 percent	3.6 percent	2.1 percent	3.4 percent	1.5 percent
7. Sound financial system	Tier 1 capital ratio stood at 10.2 percent, and NPL 1.9 percent.	Tier 1 capital ratio stood at 10.4 percent, and NPL 1.4 percent.	Tier 1 capital ratio stood at 10.7 percent, and NPL 1.2 percent.	Tier 1 capital ratio stood at 12.4 percent, and NPL 4.2 percent	Tier 1 capital ratio stood at 11.9 percent, and NPL 4.3 percent	Tier 1 capital ratio stood at 17.8 percent, and NPL 4 percent	Tier 1 capital ratio stood at 14.2 percent	Tier 1 capital ratio stood at 16.8 percent, and NPL 2.4 percent	Tier 1 capital ratio stood at 11.6 percent, NPL 3.4 percent	Tier 1 capital ratio stood at 11.0 percent, NPL 3.9 percent	Tier 1 capital ratio stood at 11.8 percent, NPL 8.0 percent
8. Effective financial sector supervision	No substantial concern in supervisory framework	No substantial concern in supervisory framework	No substantial concern in supervisory framework	No substantial concern in supervisory framework	No substantial concern in supervisory framework	No substantial concern in supervisory framework	No substantial concern in supervisory framework	No substantial concern in supervisory framework	No substantial concern in supervisory framework	No substantial concern in supervisory framework	No substantial concern in supervisory framework
9. Data Transparency and integrity	SDDS Plus Adherent	SDDS Plus Adherent	SDDS Plus Adherent	SDDS subscriber	SDDS subscriber	SDDS subscriber	SDDS subscriber	SDDS subscriber	SDDS subscriber	SDDS subscriber	SDDS subscriber

2. PLL Arrangements

	Morocco 2018 PLL	N Macedonia 2022 PLL	Panama 2021 PLL	Jamaica 2023 PLL
1. ***A sustainable external position*** (EBA assessment at least "moderately weaker")	broadly in line	broadly in line	moderately stronger	broadly in line
2. ***A capital account dominated by private flows*** (share of private flows in capital flows>50 percent)	81 percent	73 percent	78 percent	75 percent
3. ***A track record of steady sovereign access to sovereign markets at favorable terms*** (issued in at least 3 of the last 5 years in the cumulative amount of at least 50 percent of the quota)	has not issued in the last five years	3 issues over the last 5 years in the amount of 1,000 percent of the quota	issued debt in each of the last 5 years in the amount of 2,160 percent of quota	issued debt in the last 5 years amounting to US$815 million (158 percent of quota)
4. ***A comfortable reserve position*** (reserves> 100 percent of ARA metric)	95 percent	106 percent	NA	117 percent
5. ***Sound public finance*** (debt sustainable with HP)	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability	Debt is sustainable with high probability
6. ***Low and stable inflation*** *(inflation in single-digits in the last 5 years, shown: average inflation in the 3 years preceding qualification)*	1.3 percent	1.7 percent	0.4 percent	6.1 percent
7. Sound financial system	Tier 1 capital ratio stood at 10.0 percent, NPL 7.5 percent	Tier 1 capital ratio stood at 15.9 percent, NPL 3.1 percent	Tier 1 capital ratio stood at 15.7 percent, NPL 2.0 percent	Capital adequacy of DTIs stood at about 14 percent
8. Effective financial sector supervision	No substantial concern in supervisory framework	No substantial concern in supervisory framework	Weaknesses in AML/CFT supervision (FATF grey list)	Weaknesses in AML/CFT supervision (FATF grey list)
9. Data Transparency and integrity	SDDS subscriber	SDDS Plus Adherent	e-GDDS participant	e-GDDS participant

Annex VI. Evaluation of the External Economic Stress Index

This annex evaluates the experience with using the external economic stress index (ESI) since the 2017 Review. It suggests that the construction of the ESI has relied on similar sources of external risks within and across arrangements, with weights varying across countries in line with differences in risk exposure. The ESI has continued to inform access and exit discussions under FCL and PLL arrangements, together with reserves levels. Going forward, further enhancements to the ESI do not seem warranted although flexibility under existing guidance could be better leveraged.

External risks informing the ESI have been broadly similar within and across arrangements, with proxy variables adapted to country circumstances. The ESI typically captures risks to *exports* and *financial flows*, with the former proxied by commodity price fluctuations for large natural resource exporters such as Mexico (oil), Colombia (oil), Chile (copper), and Peru (copper and gold) and/or by main trading partners' growth (the U.S. for Chile, Colombia, Jamaica, and Mexico; Euro area for North Macedonia and Morocco). Similarly, risks to *FDI* are captured by commodity price fluctuations for natural resource exporters or by main investing country growth. Risks to *equity and/or debt inflows* are also commonly used in the ESI, with the former usually proxied by the emerging market volatility index (VXEEM) and the latter by the change in the 10-year US Treasury yield. Other sources of external risk less widely employed include *tourism receipts* (Morocco), *imports* (Morocco and North Macedonia), and *remittances* (four out of seven countries).

The weights on proxy variables vary across members, in line with differences in country characteristics and exposure to external risks. For almost all arrangements, the weights were estimated using BoP and IIP data as a share of GDP, following the data-based approach; a model-based approach was used for Morocco's FCL. Risks to equity and debt portfolio investment flows account for 45 to 50 percent of the ESI for Colombia, Chile, Mexico, and Panama, consistent with their well-developed financial markets. Growth developments in the US and the Euro area drive the bulk of the ESI for Mexico and Morocco given strong trade, remittances, tourism, and FDI ties. External risks to the oil and copper industries contribute to a third of the ESI for Colombia and Chile, respectively. For North Macedonia and Jamaica, risks to energy and food imports account for a third and a quarter of the ESI, respectively, reflecting ramifications from the war in Ukraine. Proxy variables and associated weights remained unchanged within and across arrangements in line with best practice, except for Mexico where changes reflected data updates, and for Morocco's FCL where the US 10-year Treasury yield was substituted for the VXEEM that was used in Morocco's PLL.

The ESI continues to guide discussions of access and exit prospects, together with considerations on the availability of reserve buffers. There is evidence that improvements in the ESI and/or declines in the impact of tail risks––as captured by the difference between the ESI under the adverse and baseline scenarios—are associated with reductions in access, consistent with a country progressively exiting from the FCL/PLL, while increased risks correlate with higher or unchanged access levels. For instance, Mexico's request for a lower access in 2021 relative to 2019 was consistent with reduced external risks signaled by the ESI, while the decision to maintain access levels unchanged at both mid-term reviews were in line with still-elevated external stress. For

Colombia, the ESI showed a worsening of the external environment after the approval of the 2020 FCL, leading to an augmentation of access the same year, which was reduced under the successor arrangement in 2022 as risks abated. But the availability of reserve buffers can delink the relationship between external stress and access levels: despite the ESI pointing to continued high risks, Peru's 2022 FCL was approved at half the level of access under the 2020 arrangement given stronger reserve buffers and the authorities' strategy of gradually phasing out Peru's use of the FCL facility. Similarly, despite a deterioration in the ESI, access under Colombia's 2020 FCL was maintained at the same level as under the 2018 FCL on the back of higher external buffers.

Shortcomings identified at the 2017 Review have been broadly addressed and significant enhancements to the ESI do not seem warranted, although flexibility under current guidance could be better leveraged. The 2017 Review of the FCL and PLL flagged the lack of comparability of the ESI shock scenarios across countries as an area of improvement; this has been addressed under subsequent FCL and PLL arrangements. Systemic leveraging of the latest WEO downside scenario, GFSR, or G-RAM to construct the ESI has facilitated better comparability of the ESI downside scenarios across countries with arrangements in place around the same period. Since the last review, the use of older vintages has been rare and, when used, duly justified in line with good practice. Additionally, a few recent arrangements have highlighted limitations to the ESI that could be addressed through updates to proxy variables and/or weights consistent with existing guidance. For instance, the staff report (SR) for Peru's mid-term review of the 2020 FCL noted that the ESI could understate the level of economic stress given a disconnect between the external risk and its proxy, as Peru's exports of non-mineral goods and services (including tourism) are expected to lag global growth, their proxy in the ESI, following the pandemic shock. In the same vein, Morocco's SRs under the PLL indicated that the ESI did not include a proxy for geopolitical risk, which could lead to more benign stress levels than reality. Updates to weights and/or proxy variables, together with clear justification, could be encouraged to accommodate country-specific developments as warranted.

Annex VI Table 1. External Stress Index, Access, and Exit under FCL and PLL Arrangements

Source: IMF staff calculations. Averages computed across the projection period. The impact of tail risks is captured by the difference between the adverse and baseline scenario ESI series.

Annex VII. Survey Results

A. Background

A survey was launched to seek inputs from country authorities on the IMF's precautionary lending toolkit. The survey consisted of multiple-choice questions, with four sections respectively covering the FCL, PLL, SLL, and precautionary SBA, where respondents were asked to express their level of agreement with statements on the benefits of precautionary arrangements, factors making them attractive or inhibiting their use, and potential options to improve their effectiveness. The survey also collected the authorities' views on exit from the FCL, the reasons behind concentration of FCLs in Latin America (and limited take-up elsewhere), and on how the IMF's precautionary arrangements compare with alternative financing through bilateral swap lines (BSLs) and regional financing arrangements (RFAs).

The survey was circulated to authorities from 91 member countries perceived as potential users of precautionary arrangements and had a response rate of 29 percent. The survey targeted borrower countries, broadly identified as emerging market and developing economies (EMDEs, as per WEO definition) that are not PRGT-eligible,[1] not classified as fragile and conflict-affected states, and without a reserve currency.[2] The survey was sent to central banks and ministries of finance through relevant Executive Director offices, with 26 countries responding as of end-January, 2023. Participation was highest among countries in Europe and Latin America, which had response rates of 57 and 37 percent, respectively. In terms of responding institutions, central banks took the lead in completing the survey (63 percent of submissions).[3]

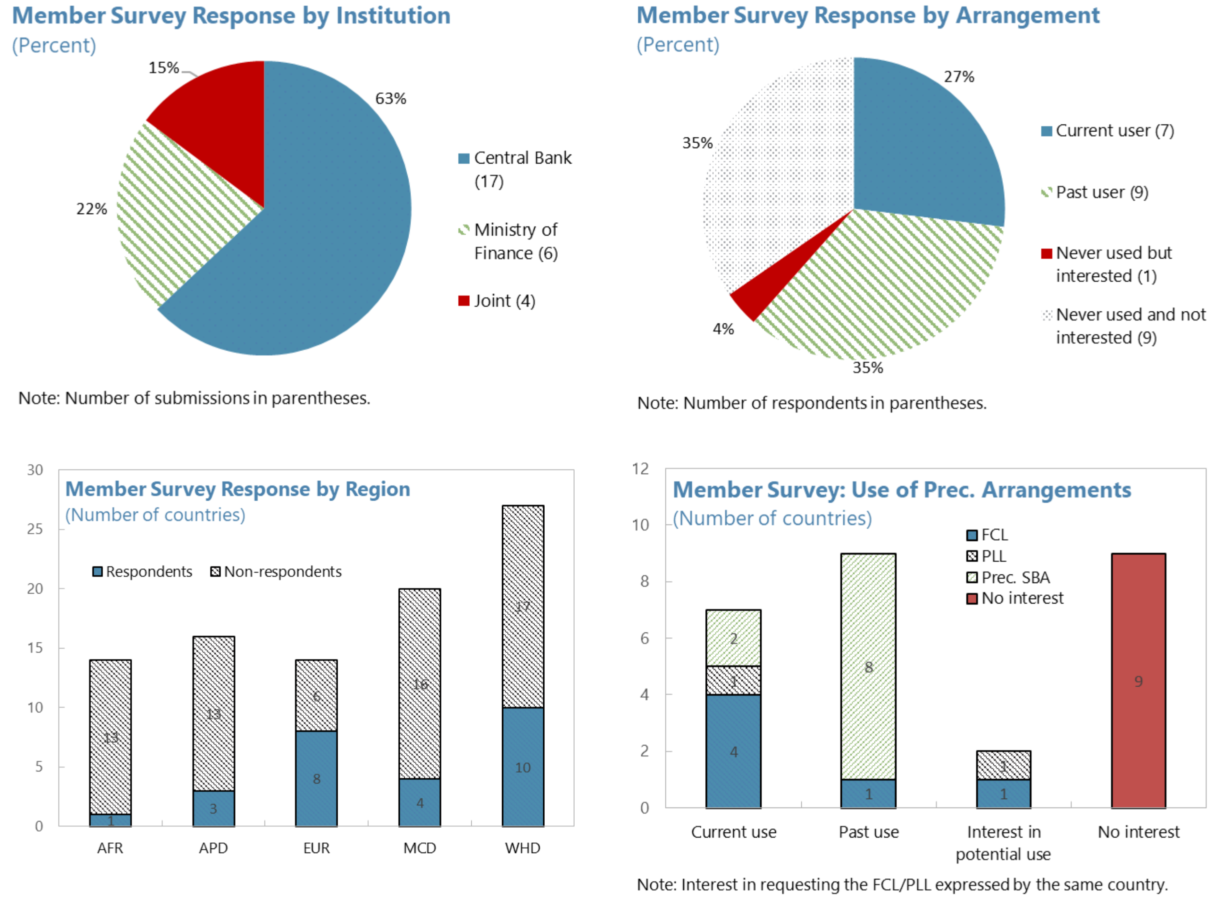
Respondents were mostly either current or past users of precautionary arrangements (64 percent of respondents). Current use is driven by the FCL (four countries), followed by the precautionary SBA (two countries), and the PLL (one country), while almost all past use is associated with the precautionary SBA (eight countries, against only one FCL). Among the ten respondents that indicated never having used IMF precautionary arrangements, only one expressed interest in potentially requesting a precautionary arrangement in the future (either an FCL or PLL), while the rest expressed no interest.

[1] Except presumed blenders, which could access the precautionary SBA with a precautionary SCF.

[2] While the survey focuses on EMDEs as potential users of precautionary arrangements, advanced economies' views could also inform the 2023 Review of the FCL, SLL, and PLL through outreach among relevant Executive Directors (ED)'s offices.

[3] Separate submissions from the central bank and the ministry of finance were received for one country, hence average responses were used in the analysis.

Annex VII Figure 1. Survey Participation



Note: AFR: sub-Saharan Africa; APD: Asia and Pacific; EUR: Europe; MCD: Middle East and Central Asia; WHD: Latin America.

B. Key Stylized Facts[4]

Benefits. The survey finds that the Fund's precautionary arrangements have served countries well, with users benefiting from strengthened foreign reserves, contained market borrowing costs, and a commitment mechanism to maintaining improved macroeconomic stability and policy frameworks.

Attractiveness. Respondents agree that upfront access to financing is an attractive feature common to the FCL, SLL, and PLL, and appreciate the flexibility in using the PLL and SBA on a precautionary or

[4] To preserve the confidentiality of survey responses, only the average level of agreement of respondents is presented for each statement, computed either over the entire sample of respondents or the sub-sample of those countries that are current or past users of precautionary arrangements. The results for the SLL sub-sample were not plotted since only one country (Chile) has used the SLL so far. The results for the PLL sub-sample reflect responses by one country.

disbursing basis depending on the balance of payments (BoP) need. For the FCL, the absence of ex post conditionality and use by only countries with very strong fundamentals also stand out as the top attractive features. The SLL continues to be an attractive instrument, including due to its revolving nature. Users also value the extension of an offer by the IMF, instead of the qualifying members requesting it. A key attractive feature of the PLL is its perception as a graduating instrument from the SBA, while users of the precautionary SBA consider its strong policy signaling important.

Factors inhibiting take-up. For the FCL, market reaction if the country is assessed as not qualifying at the mid-term review (for two-year FCLs) is the top concern undermining take-up, followed by users' preference for self-insurance through reserve accumulation, and an expectation of exit from the arrangement. For the SLL, low access, and absence of concurrent use with the FCL are perceived as limiting usage. For the precautionary SBA, users see access to alternative financing (e.g., RFAs, BSLs, donor financing), countries' preference for self-insurance through reserve accumulation, and limited awareness of the instrument's benefits among the countries and market participants as important factors inhibiting take-up. Respondents do not seem to have a strong position on factors undermining PLL usage. Overall, stigma associated with the use of Fund resources does not stand out as the top concern.

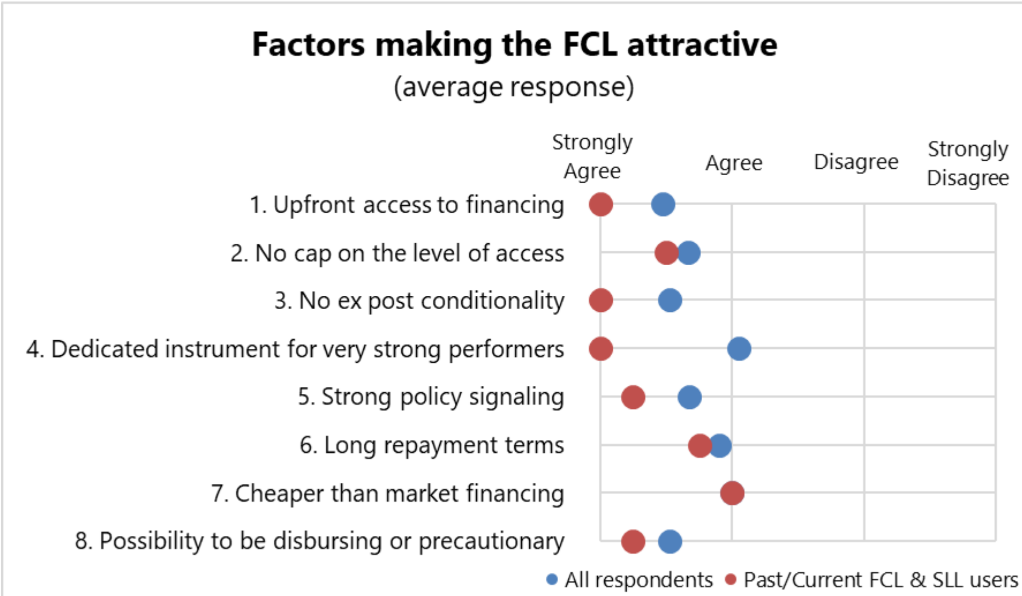
Improving effectiveness. There is strong agreement that strengthening IMF outreach to authorities, public opinion, and international markets would improve the effectiveness of the Fund's precautionary arrangements. The survey suggests that concurrent use with the FCL is a top reform that could make the SLL more attractive, together with higher access. It also indicates that pre-qualifying potential FCL and SLL users for a given time period could help. For the PLL, increasing the duration under the standard window and the access limit are among the top reforms that could enhance effectiveness**.**

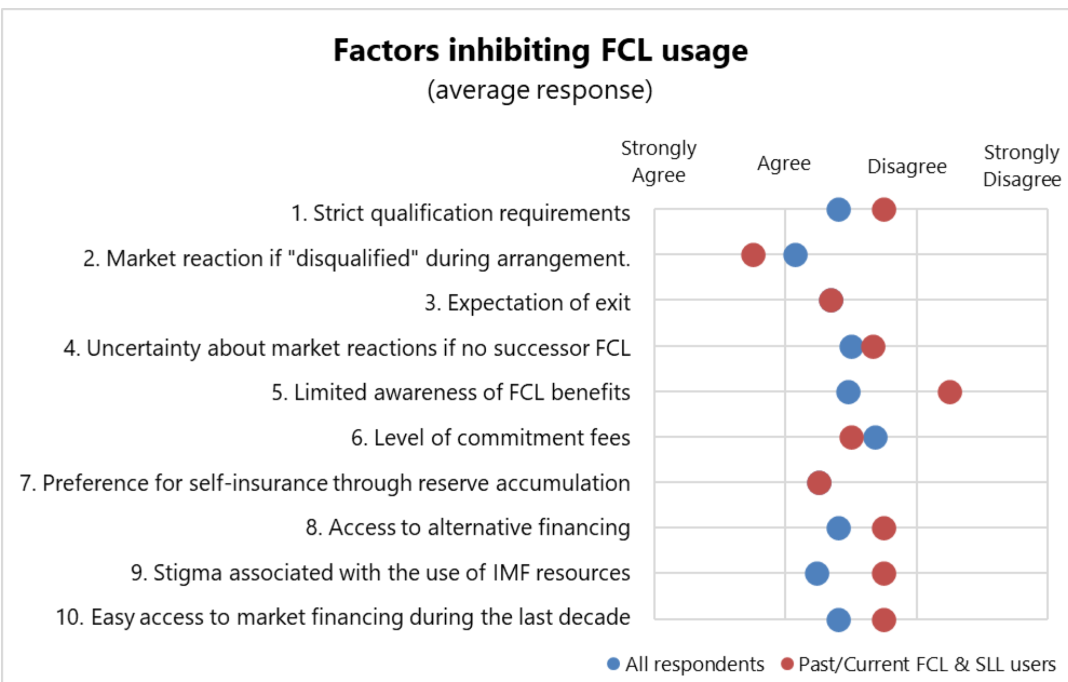
BSLs and RFAs. The survey finds limited support for the claim that BSLs and RFAs are more attractive than the FCL and SLL. However, there is some evidence that such alternative sources of financing could be perceived as more attractive than the PLL as they carry less stigma and no ex post conditionality.

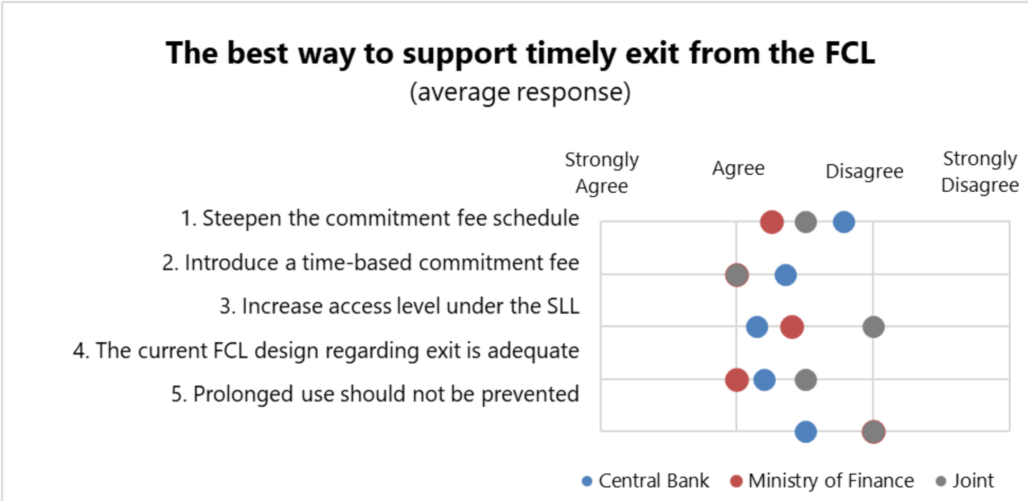
FCL exit. Users agree that increasing the level of access under the SLL could make it a more attractive exit instrument for the FCL. The member survey suggests, however, limited appetite among FCL users for introducing a time-based commitment fee or steepening the commitment fee schedule.

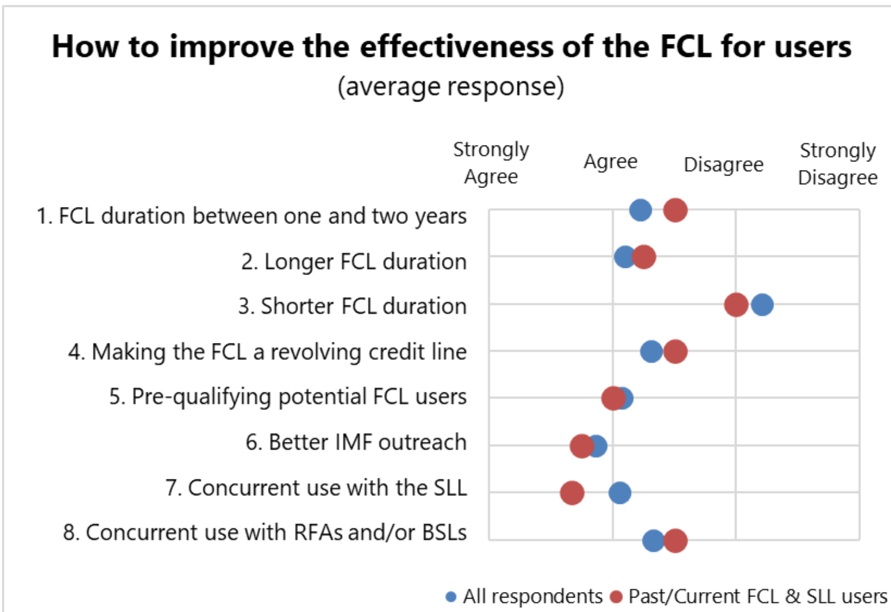
FCL regional concentration. There is indication that the uneven distribution of FCLs across regions, including concentration in Latin America, is mainly due to varying access to alternative financing instruments—such as RFAs, BSLs, and donor financing—influencing the incentive to request an FCL. Differences in the strength of fundamentals, institutions, and policies, that could be thought as leading to different likelihoods of meeting the FCL's ex ante qualification requirements, do not seem to play a role according to FCL users.

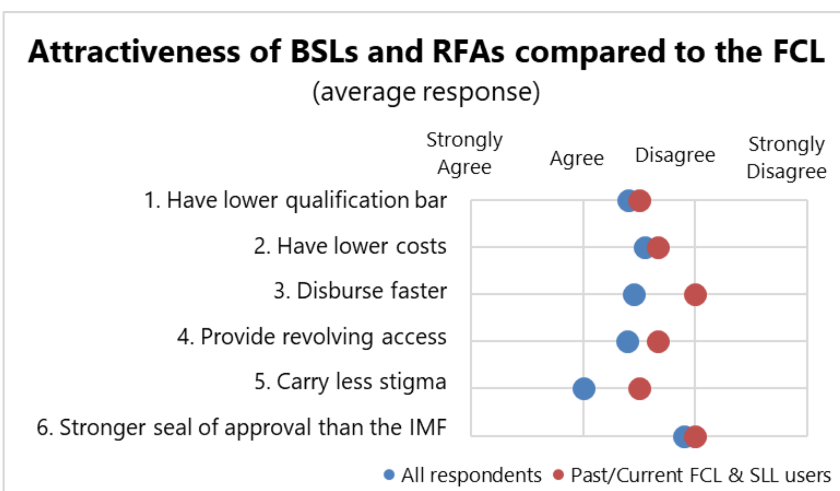
C. Charts

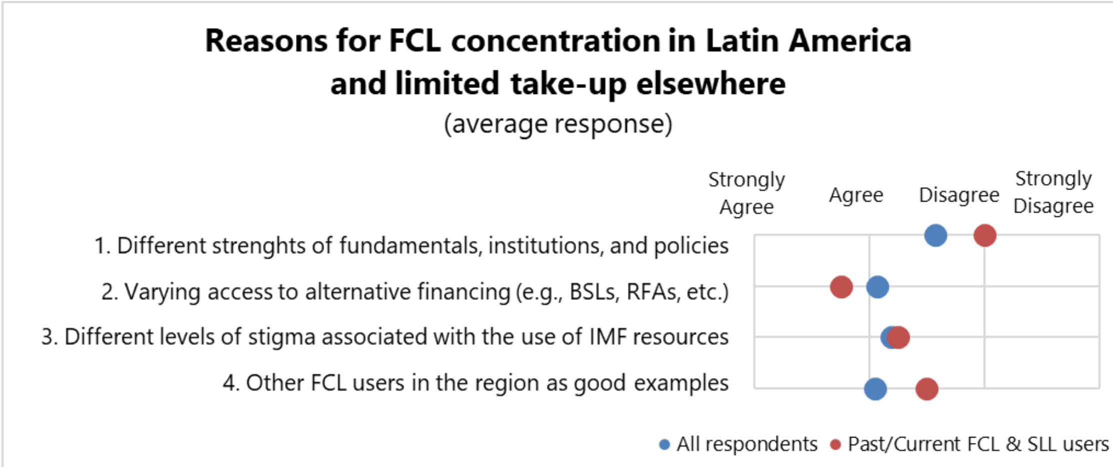

Factors making the FCL attractive
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Upfront access to financing
2. No cap on the level of access
3. No ex post conditionality
4. Dedicated instrument for very strong performers
5. Strong policy signaling
6. Long repayment terms
7. Cheaper than market financing
8. Possibility to be disbursing or precautionary
All respondents
Past/Current FCL & SLL users

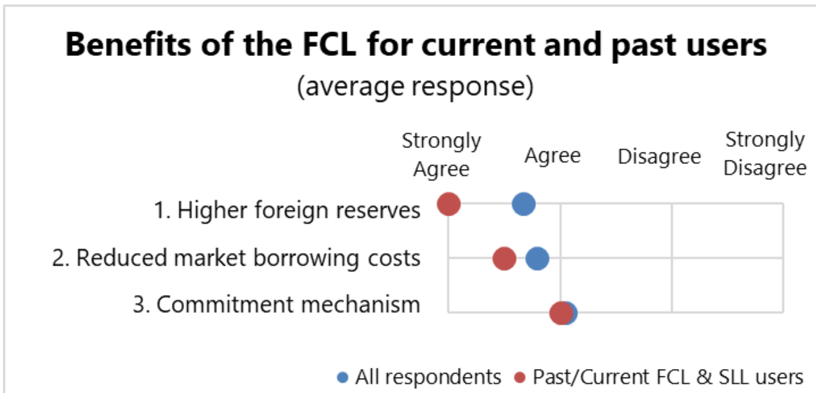

Factors inhibiting FCL usage
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Strict qualification requirements
2. Market reaction if "disqualified" during arrangement.
3. Expectation of exit
4. Uncertainty about market reactions if no successor FCL
5. Limited awareness of FCL benefits
6. Level of commitment fees
7. Preference for self-insurance through reserve accumulation
8. Access to alternative financing
9. Stigma associated with the use of IMF resources
10. Easy access to market financing during the last decade
All respondents
Past/Current FCL & SLL users

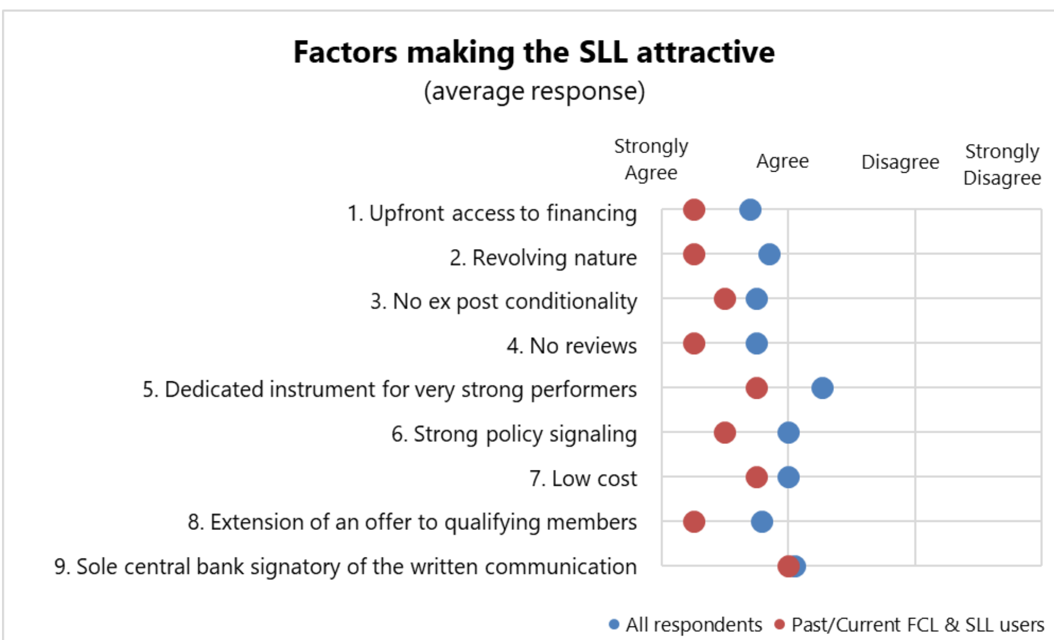

The best way to support timely exit from the FCL
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Steepen the commitment fee schedule
2. Introduce a time-based commitment fee
3. Increase access level under the SLL
4. The current FCL design regarding exit is adequate
5. Prolonged use should not be prevented
Central Bank
Ministry of Finance
Joint

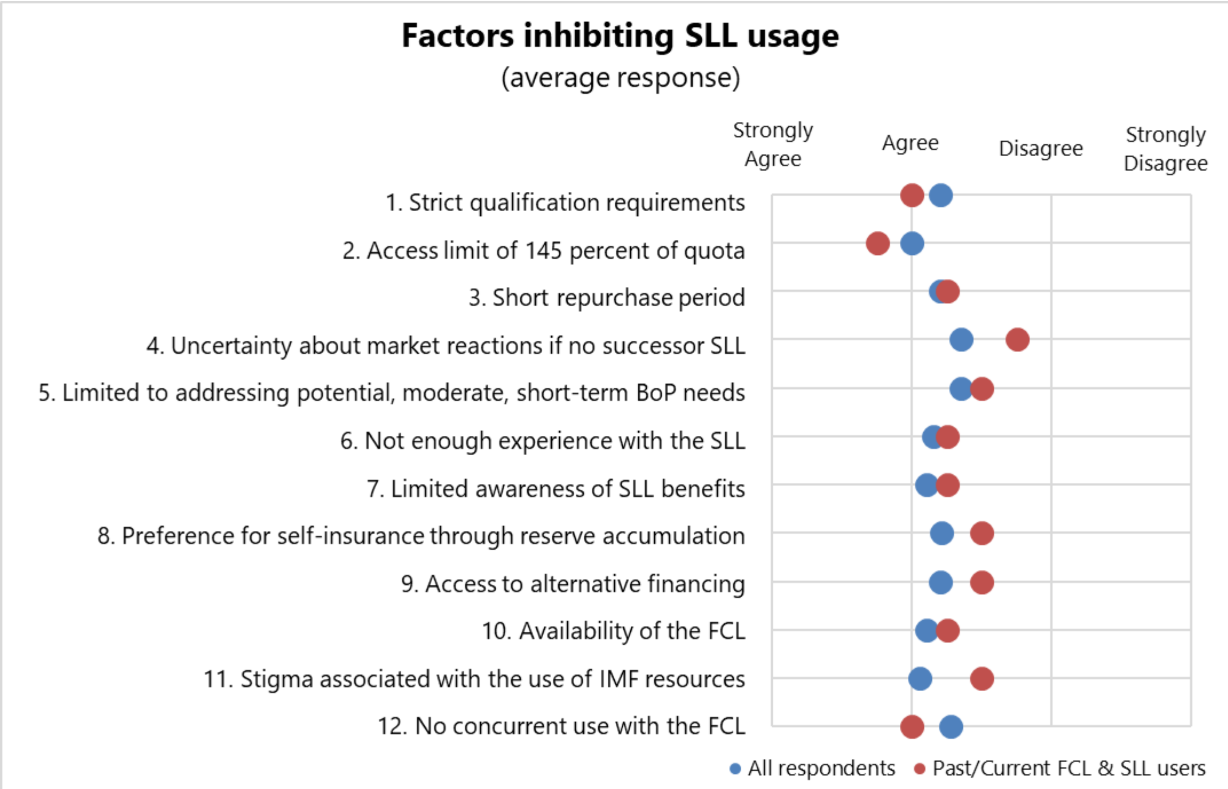

How to improve the effectiveness of the FCL for users
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. FCL duration between one and two years
2. Longer FCL duration
3. Shorter FCL duration
4. Making the FCL a revolving credit line
5. Pre-qualifying potential FCL users
6. Better IMF outreach
7. Concurrent use with the SLL
8. Concurrent use with RFAs and/or BSLs
All respondents
Past/Current FCL & SLL users

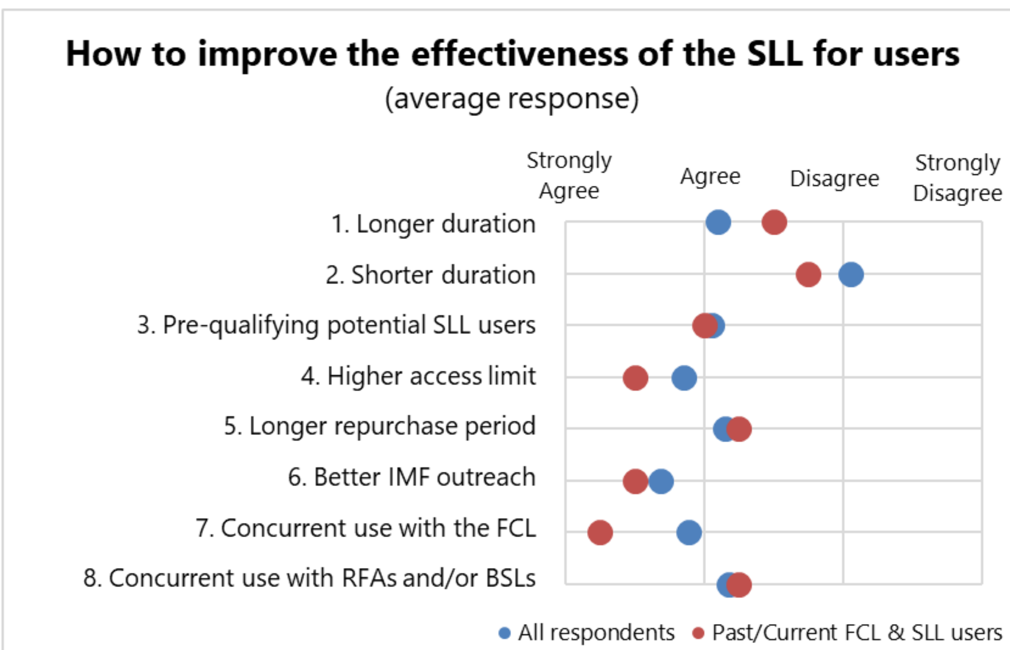

Attractiveness of BSLs and RFAs compared to the FCL
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Have lower qualification bar
2. Have lower costs
3. Disburse faster
4. Provide revolving access
5. Carry less stigma
6. Stronger seal of approval than the IMF
All respondents
Past/Current FCL & SLL users

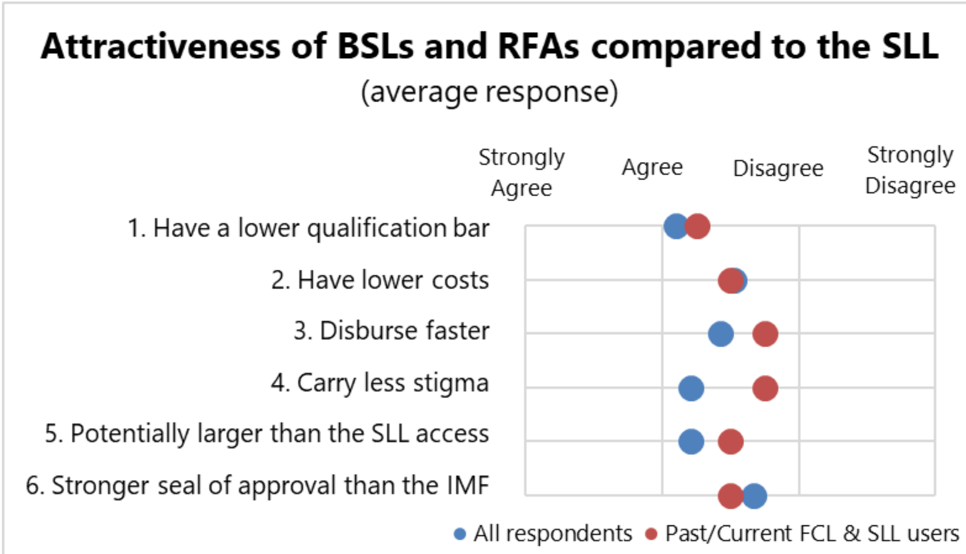

Reasons for FCL concentration in Latin America and limited take-up elsewhere
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Different strenghts of fundamentals, institutions, and policies
2. Varying access to alternative financing (e.g., BSLs, RFAs, etc.)
3. Different levels of stigma associated with the use of IMF resources
4. Other FCL users in the region as good examples
All respondents
Past/Current FCL & SLL users

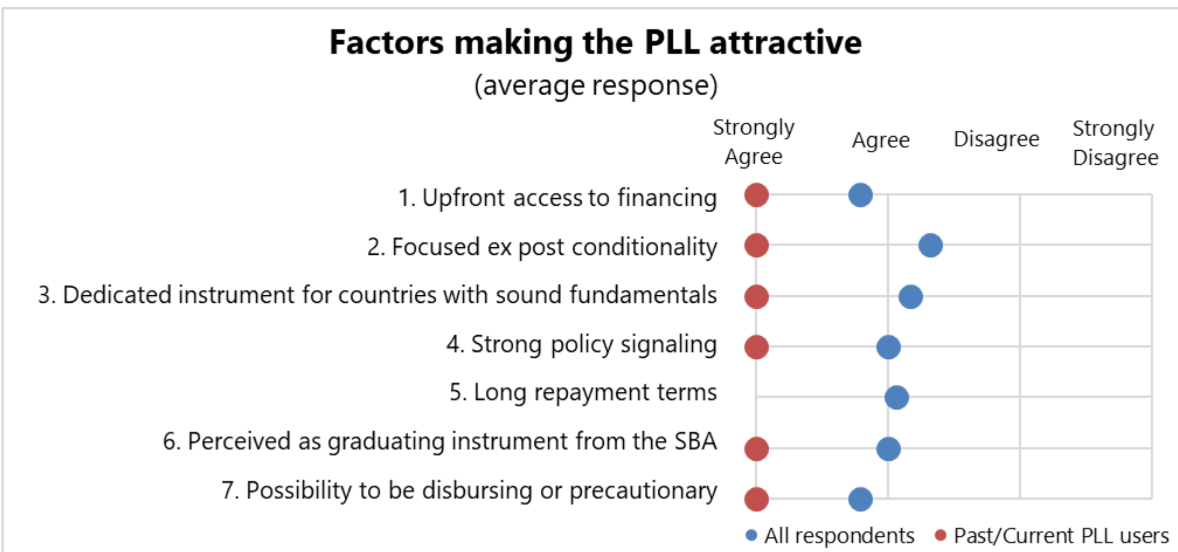

Benefits of the FCL for current and past users
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Higher foreign reserves
2. Reduced market borrowing costs
3. Commitment mechanism
All respondents
Past/Current FCL & SLL users

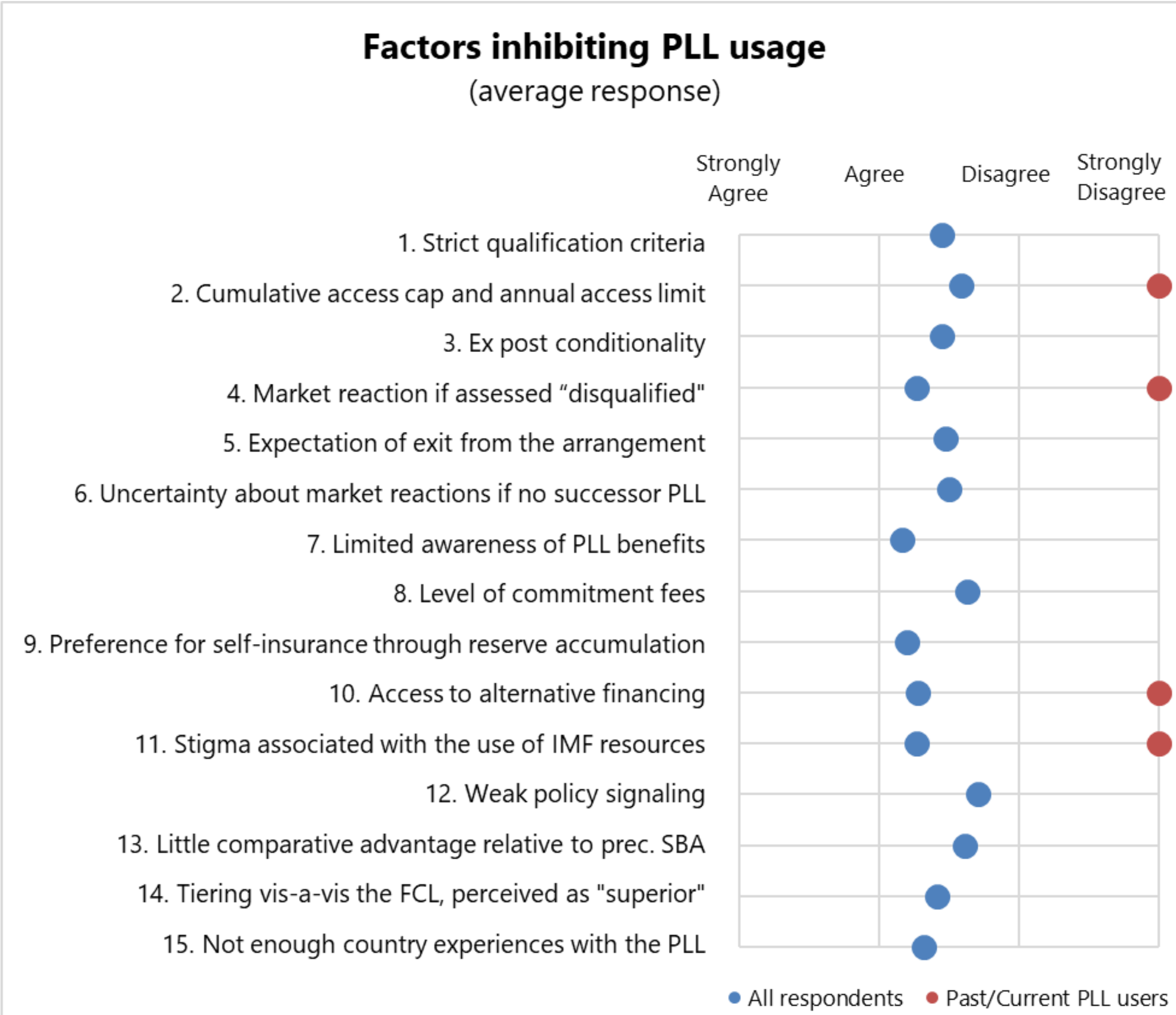

Factors making the SLL attractive
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Upfront access to financing
2. Revolving nature
3. No ex post conditionality
4. No reviews
5. Dedicated instrument for very strong performers
6. Strong policy signaling
7. Low cost
8. Extension of an offer to qualifying members
9. Sole central bank signatory of the written communication
All respondents
Past/Current FCL & SLL users

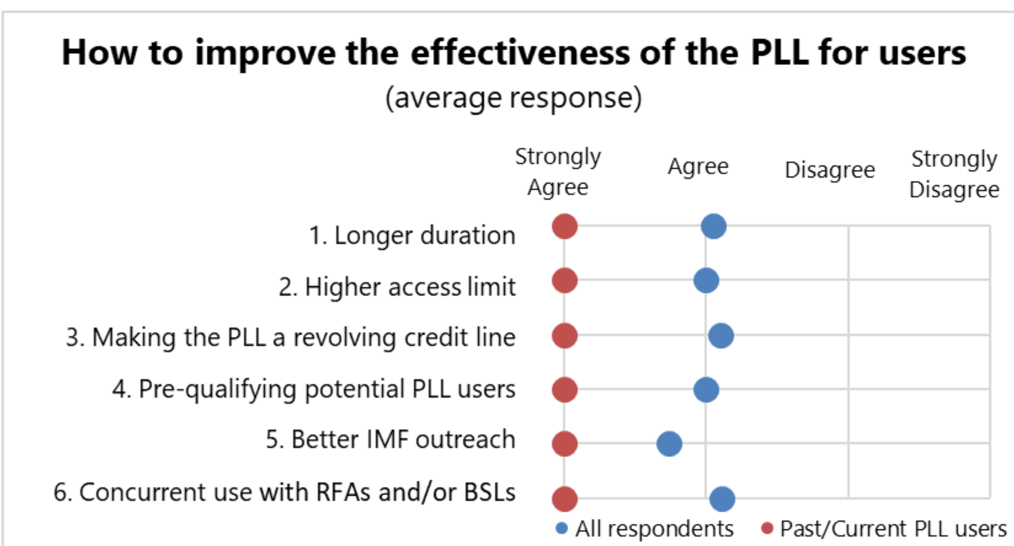

Factors inhibiting SLL usage
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Strict qualification requirements
2. Access limit of 145 percent of quota
3. Short repurchase period
4. Uncertainty about market reactions if no successor SLL
5. Limited to addressing potential, moderate, short-term BoP needs
6. Not enough experience with the SLL
7. Limited awareness of SLL benefits
8. Preference for self-insurance through reserve accumulation
9. Access to alternative financing
10. Availability of the FCL
11. Stigma associated with the use of IMF resources
12. No concurrent use with the FCL
All respondents
Past/Current FCL & SLL users

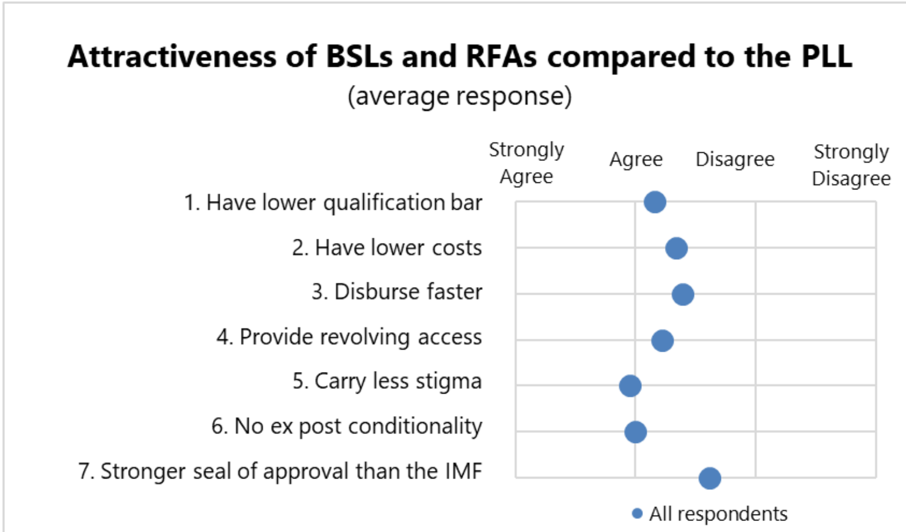

How to improve the effectiveness of the SLL for users
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Longer duration
2. Shorter duration
3. Pre-qualifying potential SLL users
4. Higher access limit
5. Longer repurchase period
6. Better IMF outreach
7. Concurrent use with the FCL
8. Concurrent use with RFAs and/or BSLs
All respondents
Past/Current FCL & SLL users

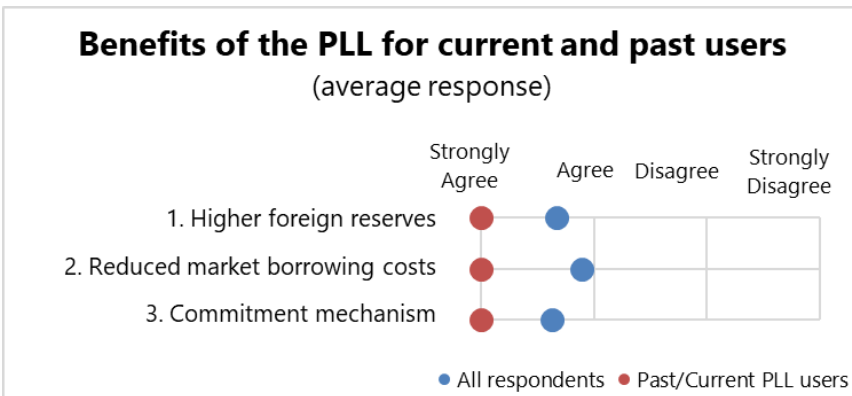

Attractiveness of BSLs and RFAs compared to the SLL
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Have a lower qualification bar
2. Have lower costs
3. Disburse faster
4. Carry less stigma
5. Potentially larger than the SLL access
6. Stronger seal of approval than the IMF
All respondents
Past/Current FCL & SLL users

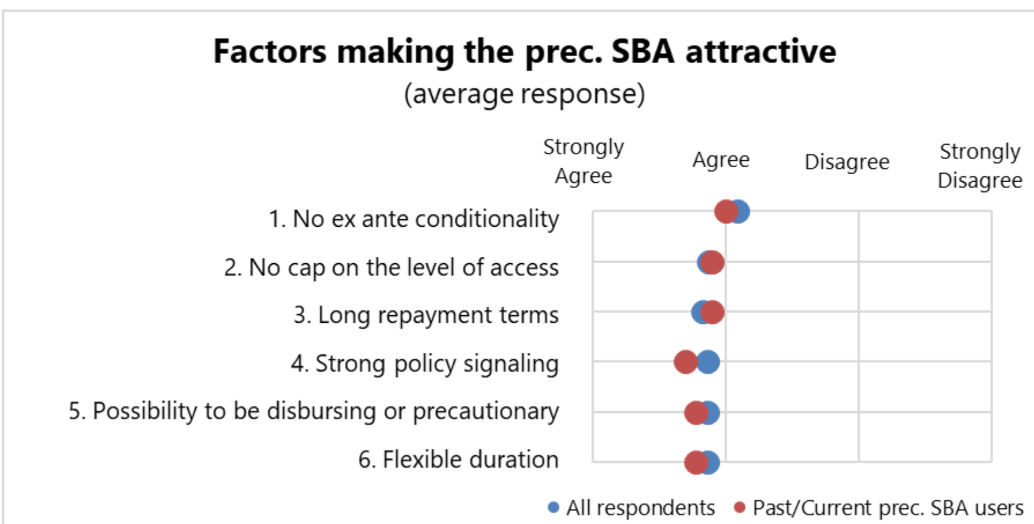

Factors making the PLL attractive
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Upfront access to financing
2. Focused ex post conditionality
3. Dedicated instrument for countries with sound fundamentals
4. Strong policy signaling
5. Long repayment terms
6. Perceived as graduating instrument from the SBA
7. Possibility to be disbursing or precautionary
All respondents
Past/Current PLL users

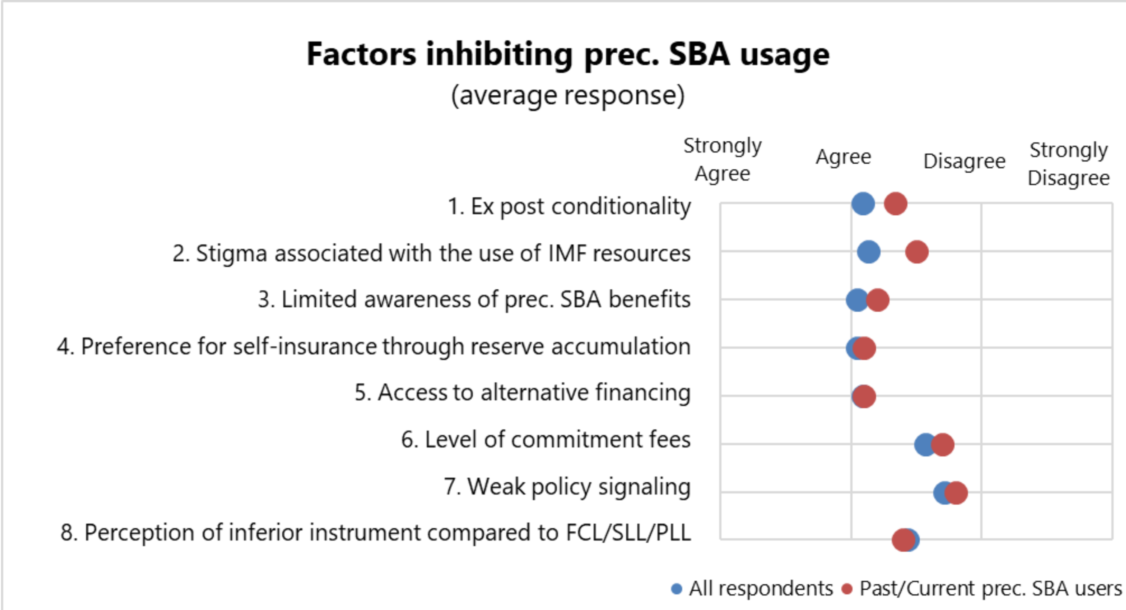

Factors inhibiting PLL usage
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Strict qualification criteria
2. Cumulative access cap and annual access limit
3. Ex post conditionality
4. Market reaction if assessed "disqualified"
5. Expectation of exit from the arrangement
6. Uncertainty about market reactions if no successor PLL
7. Limited awareness of PLL benefits
8. Level of commitment fees
9. Preference for self-insurance through reserve accumulation
10. Access to alternative financing
11. Stigma associated with the use of IMF resources
12. Weak policy signaling
13. Little comparative advantage relative to prec. SBA
14. Tiering vis-a-vis the FCL, perceived as "superior"
15. Not enough country experiences with the PLL
All respondents
Past/Current PLL users

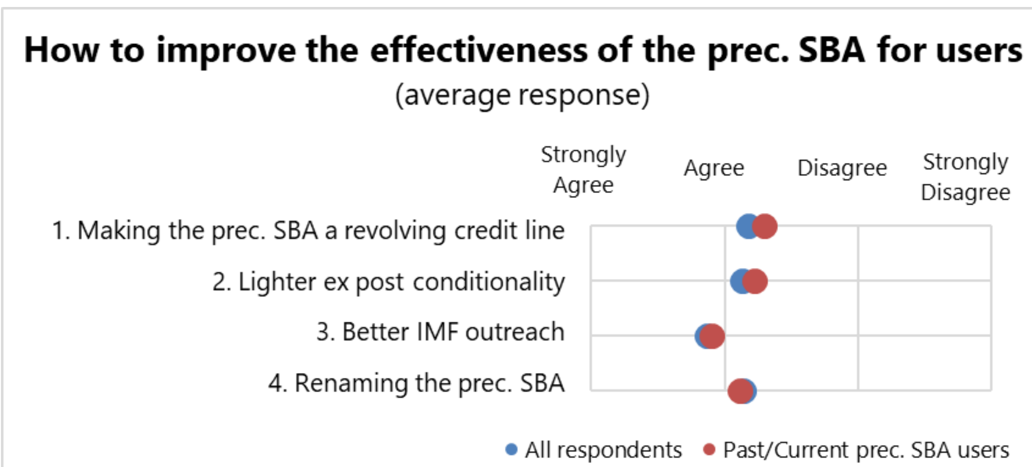

How to improve the effectiveness of the PLL for users
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Longer duration
2. Higher access limit
3. Making the PLL a revolving credit line
4. Pre-qualifying potential PLL users
5. Better IMF outreach
6. Concurrent use with RFAs and/or BSLs
All respondents
Past/Current PLL users

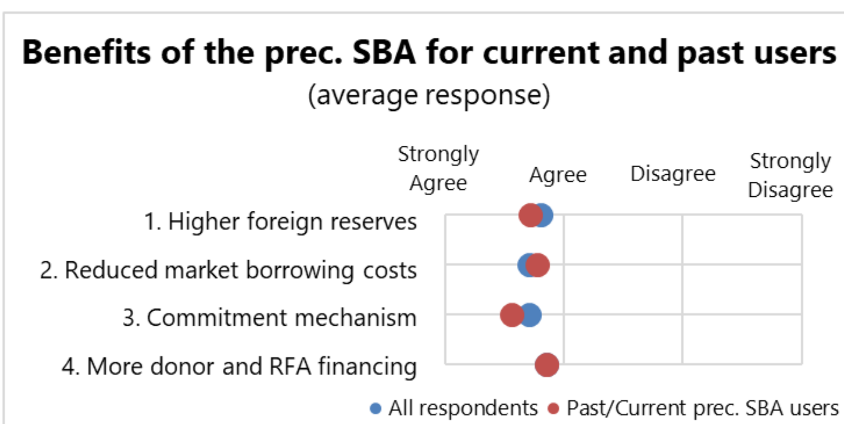

Attractiveness of BSLs and RFAs compared to the PLL
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Have lower qualification bar
2. Have lower costs
3. Disburse faster
4. Provide revolving access
5. Carry less stigma
6. No ex post conditionality
7. Stronger seal of approval than the IMF
All respondents


Benefits of the PLL for current and past users
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Higher foreign reserves
2. Reduced market borrowing costs
3. Commitment mechanism
All respondents
Past/Current PLL users


Factors making the prec. SBA attractive
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. No ex ante conditionality
2. No cap on the level of access
3. Long repayment terms
4. Strong policy signaling
5. Possibility to be disbursing or precautionary
6. Flexible duration
All respondents
Past/Current prec. SBA users


Factors inhibiting prec. SBA usage
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Ex post conditionality
2. Stigma associated with the use of IMF resources
3. Limited awareness of prec. SBA benefits
4. Preference for self-insurance through reserve accumulation
5. Access to alternative financing
6. Level of commitment fees
7. Weak policy signaling
8. Perception of inferior instrument compared to FCL/SLL/PLL
All respondents
Past/Current prec. SBA users


How to improve the effectiveness of the prec. SBA for users
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Making the prec. SBA a revolving credit line
2. Lighter ex post conditionality
3. Better IMF outreach
4. Renaming the prec. SBA
All respondents
Past/Current prec. SBA users


Benefits of the prec. SBA for current and past users
(average response)
Strongly Agree
Agree
Disagree
Strongly Disagree
1. Higher foreign reserves
2. Reduced market borrowing costs
3. Commitment mechanism
4. More donor and RFA financing
All respondents
Past/Current prec. SBA users

Annex VIII. Time-Based Commitment Fees: Revisiting Reform Options

The 2017 review of precautionary facilities explored—but did not adopt—time-based commitment fees (TBCFs) as an option for strengthening incentives to exit precautionary arrangements. This annex reviews design issues for a possible TBCF in light of more recent experiences with precautionary arrangements. Under a TBCF with the same parameters as the 2017 proposal, current users of precautionary arrangements would not incur additional fee in the immediate future, as all prolonged users have access levels below the hypothetical threshold considered. The annex does not propose to introduce a TBCF. Introducing a TBCF at the current juncture of elevated global vulnerabilities would weaken the responsiveness of the Fund's toolkit to membership's needs by making exit time- rather than state-dependent. The annex also explores reducing the commitment fee for low-access arrangements in order to encourage entry of additional qualifying members, but does not propose this in view of the negative impact on the Fund's income.

Context

1. **In recent years, a number of Directors have called for strengthening exit incentives from prolonged use of Fund's precautionary facilities at high access levels.** Such an approach would aim to preserve the revolving nature of Fund resources. When this issue was last discussed in the context of the 2017 Review of the FCL and PLL ("2017 Review"),[1] views were divided. Most Directors remained concerned about the prolonged use of high-access precautionary arrangements and thus saw scope for strengthening price-based incentives to exit. Many of them saw merit in introducing time-based commitment fees, some favored steepening the commitment fee structure to discourage unnecessarily high precautionary access, and a few saw scope for a combination of both options. Some other Directors reiterated that exit should continue to be state-dependent and did not see a case for stronger price-based incentives. Directors emphasized the need to ensure that staff reports for successor arrangements are explicit about the expectation of exit and exit strategies.

2. **Large commitments on a precautionary basis, maintained for extended periods, entail costs to the membership.** Specifically, prolonged use of large arrangements on a precautionary basis ties up a significant share of the Fund's limited resources. It can also entail costs to creditor members in the Financial Transactions Plan (FTP) that are required to maintain liquid assets to meet potential calls for drawings under such arrangements, and thus forgo revenues from investing their reserves in longer-maturity assets bearing higher interest.

3. **On the other hand, in the current global context, there may be a stronger case for the Fund to continue insuring qualifying member countries against external shocks while**

[1] "*Adequacy of the Global Financial Safety Net—Review of the Flexible Credit Line and Precautionary and Liquidity Line, and Proposals for Toolkit Reform*," *SM/17/40 (06/02/2017).*

incentivizing strong policies. Global liquidity, previously abundant, is now under pressure from the ongoing monetary policy tightening by major central banks, as well as by the normalization of fiscal policies that delivered unprecedented support during the pandemic. This, combined with a worsening global outlook, could raise potential balance of payment needs, including among members with strong policies.

4. Against this background, this annex analyzes implications of strengthening exit incentives through TBCFs. The 2017 Review explored both the options of steepening the commitment fee schedule for all arrangements and TBCFs targeted to address prolonged use of high-access precautionary arrangements. The former option would have several drawbacks. As the new structure of charges would apply uniformly to all GRA arrangements irrespective of whether these are treated as precautionary, it could also have implications for large drawing arrangements that go off-track.[2] More broadly, it would imply a tightening of Fund lending policies at a time when members' potential balance of payments and financing needs are increasing. This annex focuses instead on TBCFs targeted to prolonged use of high-access precautionary arrangements. It also considers a reform involving both targeted TBCFs to incentivize exit from prolonged use of high-access precautionary arrangements and a reduced commitment fee applicable at lower access levels to encourage entry of additional qualifying members to precautionary arrangement use. Given the current global context of elevated vulnerabilities and tighter financial conditions, this annex does not explore tighter options for TBCFs than those considered for the targeted TBCFs in the 2017 Review, and similarly proposes not to introduce a TBCF at this juncture.

Commitment Fees in Fund Arrangements

5. A commitment fee is charged under all GRA arrangements. Its rationale is to compensate the IMF for the cost of processing potential lending arrangements and for committing resources that would otherwise be available for other uses. It also meant to ensure that resources are not tied-up unnecessarily. An up-front commitment fee applies to the amount available for purchase under GRA arrangements (SBA, EFF, PLL, or FCL) that may be purchased during each annual period. This fee is refunded on a proportional basis as purchases are made under the arrangement. Reflecting the expected revolving use of SLL credit, a non-refundable commitment fee is charged on SLL arrangements.

6. The rate of the commitment fee charged increases with the amounts available for purchase within each 12-month period. The aim is to discourage unnecessarily high precautionary access and contain risks to the Fund's liquidity. At the same time, commitment fees should not disincentivize members from seeking precautionary arrangements. Under the current structure, commitment fees are levied at 15 basis points a year on amounts up to 115 percent of quota; 30 basis points a year on amounts in excess of 115 percent and up to 575 percent of quota; and 60 basis points a year on amounts above 575 percent of quota (Table 4). Short-term Liquidity Line (SLL)

[2] Members under high-access drawing arrangements which go off-track for extended periods would have to pay higher fees on the amount committed for the following 12-months.

arrangements are not subject to this commitment fee structure, but instead are charged a non-refundable commitment fee of 8 basis points because of the expected revolving use of the instrument.

Annex VIII Table1. Current Structure of Commitment Fees on UCT Arrangements by Access Level[1]

Thresholds	Fee
Access up to 115 percent of quota	15 bps
Access above 115 percent of quota up to 575 of quota	30 bps
Access above 575 percent of quota	60 bps

Source: Fund staff calculations.

[1] This commitment fee structure does not apply to the SLL, on which a non-refundable commitment fee of 8 basis points is charged instead.

Exploring a Time-Based Commitment Fee (TBCF)

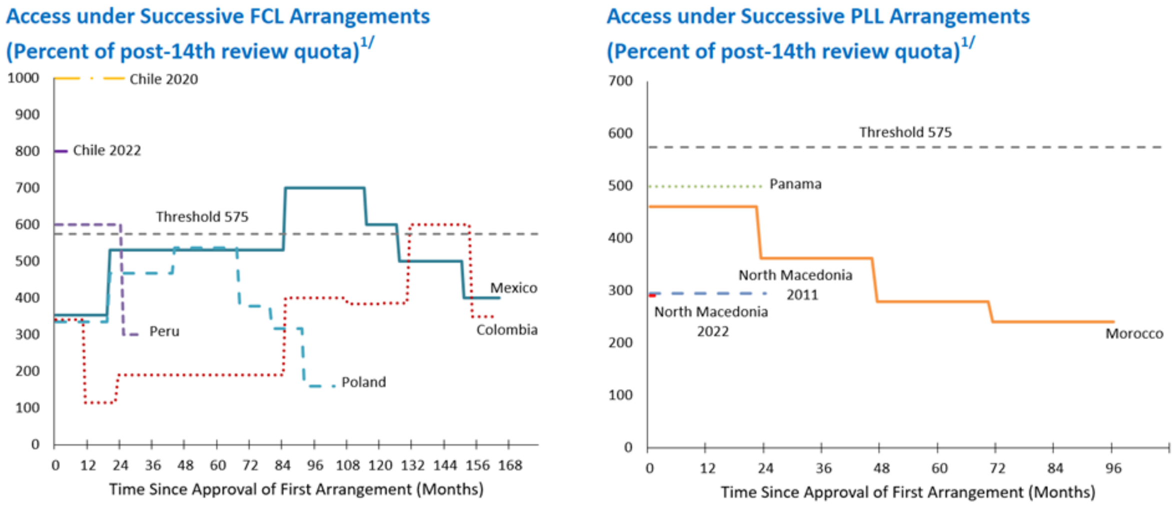
7. A TBCF would be intended to discourage large-scale prolonged precautionary lending commitments. A TBCF would make an arrangement subject to an *additional* fee once the level of undrawn credit has remained above a specified access threshold for a defined period, including under previous arrangements. Arrangements would remain subject to the fee until the level of undrawn credit falls below this threshold, through purchases, reduction of access, or upon expiration of the arrangement.[3]

8. Given the Fund's current commitment fee structure, key parameters of the TBCF reform option considered in the 2017 Review could be the starting point in reconsidering the design of a TBCF.[4] The 2017 Review explored increasing the commitment fee rate by 10–20 basis points for members with precautionary arrangements above 575 percent of quota after a set period. A lower threshold is not considered here, as it could increase the risk of member countries with a precautionary arrangement moving to lower access prematurely, when larger insurance against external shocks may still be appropriate under protracted conditions of elevated global risks.

[3] This is analogous to the application of time-based surcharges, which are levied for the period that members' credit outstanding remains above a threshold, currently set at 187.5 percent of quota. The clock toward meeting the TBCF trigger would pause once undrawn balances fall below the threshold and would reset once undrawn balances remain below the threshold for a defined continued period of time ("cooling off" period). See Appendix for details.

[4] The Box further elaborates on design issues.

Annex VIII Figure1. Access under Successive FCL Arrangements



Source: Finance Department.
1/ Total access under precautionary arrangements excludes outstanding credit.

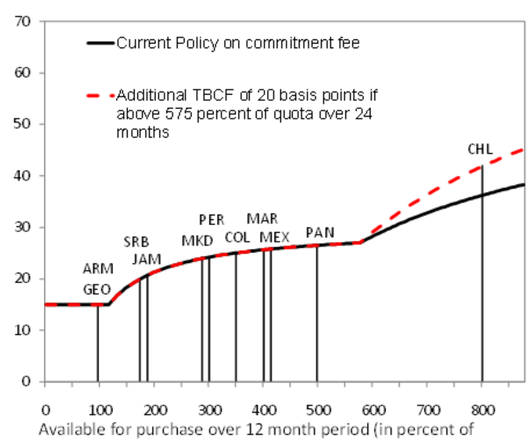
9. The 2017 review considered a higher commitment fee triggered after 48 months. This annex explores the option of triggering the higher commitment fee after 24 months, since no country so far has maintained access above 575 percent under a precautionary arrangement for more than 42 months. The 24-month period is short enough to support the revolving nature of Fund resources, and long enough to allow for periods of prolonged external stress.

10. Applying these parameters, none of the existing current precautionary arrangements would incur time-based charges for at least another 15 months, and hence they would have a limited impact on incentivizing exit in the immediate future. Currently, there is only one FCL arrangement (Chile) with an access level above 575 percent of quota, which was approved recently (August 2022) (Text Figure). Only two other FCL arrangements had access levels above 575 percent of quota in the past: (1) Mexico's FCL, for a total of 42 months between May 2016 and October 2019, with a maximum access level of 700 percent of quota; and (2) Colombia's arrangement with a maximum access level of 600 percent of quota for 24 months between May 2020 and April 2022. PLL arrangements are currently capped at an access level of 500 percent of quota, below the TBCF access threshold of 575 percent considered here. All currently active precautionary SBAs have access below 575 percent of quota.

11. A TBCF of 20 basis points above 575 percent of quota would have a small impact on the *effective rates* of commitment fees and thus limited success in incentivizing exit from precautionary arrangements. For example, if the member with the highest access (Chile, with access at 800 percent of quota) maintained such an access level for a prolonged period of time, with triggering of the time-based commitment fee, the effective (i.e., average) rate would increase from 36 to 42 basis points. This would lead to additional Fund income of SDR 7.8 million per year.[5]

12. While a TBCF could potentially be combined with a reduced commitment fee for low-access arrangements to encourage additional qualifying members to seek precautionary arrangements, this would have a negative impact on Fund's income. The take-up of precautionary arrangements has been rather low so far, especially during periods of abundant global liquidity before the start of the monetary tightening cycle in 2022. In the current environment of heightened risks, the Fund could consider making existing precautionary instruments cheaper for new users to support member countries while incentivizing strong policies. That, however, would have a negative impact on Fund income. For example, reducing commitment fees by 10 basis points for precautionary arrangements with access below 575 percent of quota, would lower commitment fee revenues by about SDR 60 million per year, or about 34 percent of the average annual commitment fees from precautionary arrangements (Table 5), though this loss could be mitigated if the lower commitment fee incentivized additional qualifying members to enter into precautionary arrangements with the Fund. In addition, since the lower commitment fees would have to apply uniformly to all GRA arrangements irrespective of whether these are treated as precautionary, there would potentially be an additional revenue loss for the Fund compared with maintaining the status quo.

Annex VIII Figure 2. Commitment Fee Effective Rates (basis points) 1/



1/ The effective rate is the total commitment fee payable relative to total access available for purchase over a 12 month period.

[5] The effective rate is the total commitment fee payable relative to total access available for purchase over a 12-month period. The total commitment fee payable is calculated using the relevant commitment fee structure. For example, for a member with access of 135 percent of quota, a commitment fee of 15 basis points is applied on 115 percent of quota, and a commitment fee of 30 basis points is applied on the remaining 20 percent of quota.

Annex VIII Table 2. Implications of Illustrative Reduction in Commitment Fees on Current FCL/PLL Arrangements

Member	Access	Current policy		10 bps decrease below 575% of quota		
	(percent of quota)	Effective rate[2] (bps)	Nominal fee[3] (million SDRs)	Effective rate[2] (bps)	Nominal fee[3] (million SDRs)	Difference in nominal fee (million SDRs)
Chile (FCL)	800	36	50.6	29	40.6	-10.0
Colombia (FCL)	350	25	17.9	15	10.8	-7.2
Mexico (FCL)	400	26	91.6	16	55.9	-35.7
Morocco (FCL)	417	29	10.6	19	6.9	-3.7
Peru (FCL)	300	24	9.7	14	5.7	-4.0
Jamaica (PLL)	190	21	1.5	11	0.8	-0.7
North Macedonia (PLL)	290	24	1.0	14	0.6	-0.4
Armenia (SBA)	100	15	0.2	5	0.1	-0.1
Georgia (SBA)	100	15	0.3	5	0.1	-0.2
Serbia (SBA)	170	20	2.2	10	1.1	-1.1
Total			185.7		122.6	-63.2

Source: IMF staff calculations.

[1] Includes arrangements current as at April 15, 2023.

[2] The effective rate is the total commitment fee payable relative to total access available for purchase over a 12-month period.

[3] Over a one-year 12-month period.

Assessment

13. Staff does not support introducing a time-based commitment fee at this time with the aim to incentivize exit as it would weaken the responsiveness of the precautionary facilities toolkit to current membership's needs. A time-based fee, albeit targeted to prolonged use of precautionary arrangements would be triggered irrespective of the state of external risks faced by members. Also, under the assumption that such a fee should not be tighter than the targeted TBCF in the 2017 Review, it would also be expected to have a limited impact on FCL exit (based on FCL experience so far). Also, this would de facto tighten policies in support of member countries at a time when global vulnerabilities are particularly elevated. Due to the legal requirement of uniformity of charges, the application would also not be restricted to arrangements that are treated as precautionary. Ramifications for the wider GRA toolkit would therefore need to be considered carefully in the design of the policy. Similarly, a targeted TBCF accompanied by a reduced commitment fee for low-access precautionary arrangements would have a significant negative impact on Fund income. Moreover, any TBCF would significantly increase the complexity of the Fund's fee structure and be operationally burdensome.

Annex VIII Box 1. Further Design Aspects of a Time-based Commitment Fee

A time-based commitment fee (TBCF) would operate similarly to the current policy on time-based surcharges and be charged on top of existing level-based commitment fees. It would apply once the level of undrawn credit for each relevant (12-month) period under successive arrangements has remained above a specified threshold for a defined duration of time ("duration trigger"). The fee would be charged only for the period when undrawn credit remained above the threshold, analogous to Fund policy on time-based surcharges. The count toward meeting the duration trigger would start as the threshold is breached and would pause whenever the level of undrawn credit falls below the threshold level, or the arrangement expires or is cancelled. The count would reset only once a "cooling-off" period is exceeded. Once triggered, the TBCF would be levied ex-post at each anniversary date of the relevant period (or at the end of the arrangement if sooner) for the time during which undrawn balances remain above the threshold.

The access threshold for a TCBF would need to be set at a sufficiently high level to appropriately target large precautionary commitments and mitigate the risks of unintended consequences. The threshold could be set, for example, at the highest level-based commitment fee threshold of 575 percent of quota. Such a high threshold could address Directors' concerns regarding particularly large and prolonged commitments, in practice applying only to protracted use of high access FCL arrangements. A lower threshold could increase the risk of member countries with a precautionary arrangement moving to lower access prematurely, when larger insurance against external shocks is still needed.

Beyond the choice of threshold levels and TBCF rates, the following design aspects would need to be considered:

- **Duration trigger.** The length of the trigger period should be short enough to effectively support the revolving nature of Fund resources, while recognizing the possibility of extended periods of stress justifying prolonged commitments. One option is to link the duration trigger to the typical length of a severe shock, i.e., around 3 or 4 years. In view of the maximum two-year duration under the current FCL arrangements, a 4-year duration trigger could be considered, effectively being applied at the beginning of the third FCL arrangement, provided access would remain above the threshold. Such long duration trigger would also significantly limit the risk of unintended ramifications across arrangements, as the level of undrawn balances is less likely to remain above the threshold for a period of four years unless the arrangement is treated as precautionary.
- **Cooling-off period.** Short intervals between successive arrangements, or purchases reducing the level of undrawn credit to below the threshold for some time, could "pause" the count toward meeting the duration trigger. The count would continue once the level of undrawn credit increases above the threshold again, for example, because of a new 12-month period starting, a successor arrangement being approved, or access being augmented. However, the count would be reset once a certain "cooling off" period is exceeded. Such a period should be long enough to effectively promote a durable exit from prolonged arrangements and ensure that delays in successor arrangements do not interfere with the policy. On the other hand, too long a cooling-off period could increase the likelihood of penalizing members that would request a successor arrangement with a delay on the basis of new external risks that were not foreseen when the previous arrangement was allowed to expire. On balance, a cooling off period when undrawn credit remains below the threshold continuously for one-year would seem appropriate.
- **Ex-post billing.** The fee could be billed and paid ex-post, at each anniversary date and upon expiration/cancellation for the period in an arrangement where commitments exceed the threshold. In the event purchases brought the level of undrawn credit below the threshold, a pro-rated TBCF would be levied at the end of the relevant period, covering only the time for which the threshold was exceeded. The same policy would be applied to cancellations and changes in the level of access under the arrangement. This implies that, in contrast to current policy on level-based commitment fees, the time-based fee, once triggered, would not be refundable against purchases.

Annex IX. Scoring of Precautionary Arrangements in the FCC

This annex revisits the Fund's practice of counting, or "scoring" of arrangements treated as precautionary at full value ("full scoring") for purposes of measuring the Fund's liquidity in the Forward Commitment Capacity (FCC). It illustrates the impact of "partial scoring" on the Fund's liquidity, and how this could delay and complicate potential activation of the Fund's borrowed resources. The annex concludes that full scoring of precautionary arrangements under the FCC remains appropriate in light of the Fund's unique mandate and financing structure. More broadly, staff does not consider partial scoring appropriate in light of the Fund's unique mandate as the "lender of last resort".

Context

1. The Fund's main measure of liquidity—the Forward Commitment Capacity (FCC)—indicates the Fund's capacity to make new financial commitments under the General Resources Accounts (GRA) over the upcoming 12 months. The FCC equals uncommitted *usable resources*[1] plus members' scheduled repurchases, less the repayments due by the Fund to its creditors (to repay resources borrowed under the New Arrangements to Borrow and/or Bilateral Borrowing Agreements), both measured over the upcoming 12 month period, minus a prudential balance. The FCC is updated and published weekly.

2. Since the inception of the FCC in 2002, commitments under arrangements treated as precautionary have been fully scored (or counted) in the FCC. Under *full scoring*, commitments under precautionary arrangements are counted at their full value for the purpose of measuring liquidity regardless of the likelihood of such resources being purchased. This ensures that resources are available to finance requests for drawings under current commitments, consistent with the Fund's mandate as the "lender of last resort". [2] Furthermore, full scoring precautionary commitments is embedded in the Fund's Borrowing Guidelines as well as in each individual bilateral borrowing agreement.[3]

[1] Usable resources from quotas consist of (i) holdings of the currencies of members considered by the Executive Board to have a sufficiently strong balance of payments and reserve position for their currencies to be used in the financing of IMF transactions, and (ii) Fund's holdings of SDRs. A "modified FCC" also includes usable resources from borrowed resources, in the event that these resources are activated (see below on activation conditions).

[2] In the Fund's Financial Transactions Plan (FTP), possible drawings under arrangements treated as precautionary during the plan period are fully covered. Providing for the full amount within the approved maximum transfers under the plan helps underpin confidence that the Fund can make all potential disbursements in a timely manner and consistent with the design of the precautionary arrangements under which large amounts may be drawn at short notice.

[3] These agreements reference the FCC decision No. 14906 (11/38), adopted on April 20, 2011. Any modifications to the FCC definition would raise the question of the need for potential changes to the NAB Decision and 2020 BBAs, and in this regard the consent of NAB participants and 2020 BBA creditors.

3. The Board reviewed the full scoring approach in 2017 in the context of the previous review of the FCL and PLL.[4] Directors generally considered that full scoring remained appropriate and supported a continuation of this approach as it provides a clear assurance that resources that have been committed will be available to members with arrangements in all circumstances. However, a few Directors saw some scope for flexibility by *partially scoring* these commitments, on the basis of the expected low probability of drawing under such arrangements and with a view to freeing up more quota resources for lending.[5]

4. This annex reviews the implications of full and partial scoring. Given the continued call by some Directors for the Fund to consider partial scoring of precautionary arrangements as an alternative to full scoring in the measurement of Fund liquidity, this annex reviews key considerations for scoring precautionary arrangements and the implications for the Fund's liquidity and the Fund's ability to activate its borrowed resources under partial scoring.

Key Scoring Considerations

5. Precautionary arrangements present uncertainty as to whether or not they will be drawn, and if so, when. Fund arrangements represent an assurance by the Fund to members that they are able to purchase the amounts committed by the Fund, subject to the terms of the arrangement. In contrast, an intention by a member to treat an arrangement as precautionary can at any time be unilaterally revisited if that the member experiences an actual BOP need. This means that at any time the member can purchase the entire amount available to it at that time under the terms of the arrangement. The timing of any potential purchase is therefore inherently uncertain.

6. Partial scoring would treat only part of the amounts under precautionary arrangements as "committed usable resources". The lower the scoring of precautionary arrangements in the FCC, the higher the level of the FCC. For example, under full scoring, the Fund's undrawn balances under GRA commitments on a precautionary basis stood at SDR 66 billion at end-FY2023. Under 50 percent partial scoring, these commitments would be scored at only SDR 33 billion, implying the FCC would be higher by the difference (in this case also SDR 33 billion).

7. Two pre-conditions for partial scoring to be feasible, flagged in the 2017 review, remain binding constraints.

i. **Are the Fund's precautionary exposures sufficiently well diversified?** For partial scoring to be feasible**,** there should be confidence that drawings under these arrangements represent only a fraction of its total commitments at any point in time and that they would not be drawn concurrently. Currently, the largest commitments under precautionary

[4] *Adequacy of the Global Financial Safety Net—Review of the Flexible Credit Line and Precautionary and Liquidity Line, and Proposals for Toolkit Reform*, SM/17/140 (6/2/2017).

[5] To acknowledge the different perspectives, from December 2017 the Fund has published the breakdown of its undrawn balances under GRA commitments on a precautionary and a non-precautionary basis.

arrangements remain concentrated in the Western Hemisphere[6]—notwithstanding the recently approved FCL arrangement for Morocco, the PLL arrangement for North Macedonia, and precautionary SBAs for Armenia and Georgia—and the risks of a correlated drawing cannot be ruled out. Moreover, even if commitments under precautionary arrangements were more geographically diversified, correlated drawings remain a risk during events with a global impact—for example, such a scenario could have arisen in 2020 following the synchronized pandemic shock, if precautionary arrangements had been in place with countries that instead requested emergency financing—or with a particular impact on emerging markets.

ii. **Does the Fund have a credible mechanism in place to mobilize the necessary resources quickly should large-scale drawings materialize?** Should there be a large call on the Fund's quota resources, borrowed resources could supplement quota resources. The New Arrangements to Borrow (NAB), the Fund's standing borrowing facility, represents the second line of defense after quotas. Bilateral borrowing agreements (BBAs) would also be potentially available, but only as a third line of defense after quotas and the NAB have been largely exhausted. However, NAB and BBA resources can be activated only subject to creditor conditions (see below)—*and cannot be used to finance purchases under commitments approved outside of the respective NAB and BBA activation periods*.[7] Moreover, legislative provisions in the U.S. described below (Annex Box 2) allow the U.S. to support a proposed NAB activation only if the FCC is expected to fall below SDR 100 billion during an activation period. The Fund cannot itself raise the FCC threshold at which borrowed resources can be activated.

8. A change in scoring could also have implications for monitoring liquidity risk under the Fund's new risk framework. Building on the 2016 Board-approved Risk Acceptance approach, the Fund's new Enterprise Risk Management (ERM) framework envisages moderate risk tolerance for the Fund's liquidity (on the basis of "moderate" risk when the FCC is above SDR 125 billion and up to SDR 175 billion).[8] The new approach entails a notification to the Board when the FCC falls to SDR 125 billion. Partial scoring would increase the FCC, but imply a change in underlying risk tolerance and delay risk mitigation measures (e.g. activation of borrowed resources with creditor consents).

9. A shift to partial scoring would undermine the Fund's liquidity and recourse to borrowed resources. Partial scoring would not increase the Fund's overall resource envelope, but could lead to a situation where the Fund would commit more resources to members than it would

[6] See *Review of the Adequacy of the Fund's Precautionary Balances*, SM/22/260 (11/16/2022).

[7] The Fund's current BBAs, the 2020 BBAs, can be activated only if—among other conditions—the NAB is also already activated or there are no available uncommitted NAB resources.

[8] See *Enterprise Risk Management—Proposed Risk Tolerance Statements and Risk Tolerance Levels* – Supplementary Information (FO/DIS/23/3, sup 1).

have available to meet simultaneous drawings from all members with precautionary arrangements. This could be especially problematic in the event of a significant global shock:

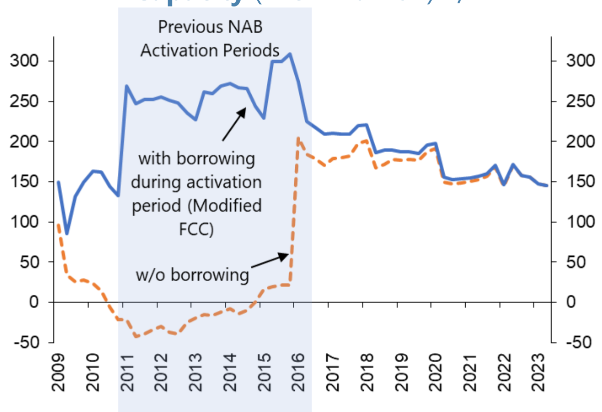
- ***Delayed access to borrowed resources***. Partial scoring would immediately increase the FCC but without any corresponding change in actual resources (liquidity) available for lending. The FCC would become a misleading indicator of the Fund's ability to commit new resources. Because activation of the Fund's borrowed resources depends on the outlook for the level of the FCC (Annex Box 2), partial scoring would therefore delay and complicate activation of the NAB and/or BBAs, thereby potentially compounding liquidity risks for the Fund. In extreme circumstances, partial scoring could lead to risk of the Fund overcommitting *all* of its resources (both quota and borrowed).

- ***Overcommitting quota resources***. In turn, a delay in the activation of borrowed resources due to partial scoring would imply making potentially larger commitments based on quota resources than under full scoring. In the scenario shown below, if the NAB were to be activated at a later stage, the Fund could even be left without sufficient quota resources to allow for adequate co-financing of new commitments, thus potentially precluding the Fund from using its borrowed resources and more than halving the Fund's overall resources envelope.

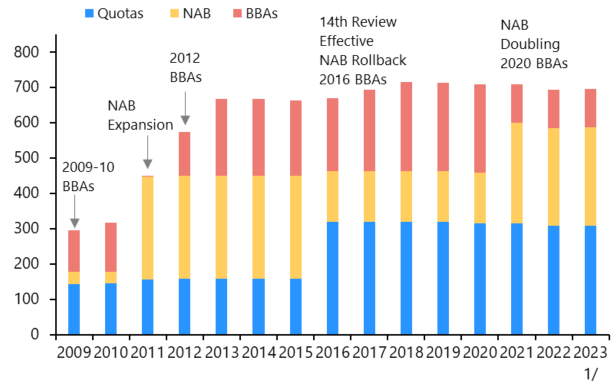
- ***Diminished credibility of Fund as "lender of last resort"***. There is a risk that, if there were any doubts about the Fund's ability to meet its commitments made under arrangements in case actual BOP needs emerge, the confidence-enhancing effect of precautionary arrangements may diminish, and consequently the incentives for members to rely on such facilities instead of accumulating excess reserves could wane. Such doubts could also create incentives for members to rush to draw down their precautionary arrangements to ensure early access to the Fund's limited pool of resources, directly undermining confidence rather than instilling it. Particularly in a context of a global stress scenario, partial scoring could lead to inadequate Fund liquidity and thus directly undermine the Fund's role as a global "lender of last resort".

Annex IX Box 1. Activation of Borrowed Resources

Annex Figure 7A: Forward Commitment Capacity (in SDR billion) 1/



Annex Figure 7B: Lending Capacity (in SDR billion) 1/



The NAB and BBAs currently account for a majority of the Fund's aggregate lending capacity. Borrowed resources currently represent around 55 percent of the Fund's lending capacity. They contribute about SDR 278 billion (NAB) and SDR 108 billion (BBAs) to the total lending capacity of SDR 695 billion (around US$936 billion) as of end-April 2023. Borrowed resources are, however, available for lending only for commitments made by the Fund during periods in which these resources were activated in accordance with their respective procedures (including creditor consents). The Fund has not activated the NAB since 2016, and the 2020 BBAs have never been activated, despite the impact of the pandemic from 2020 and other subsequent shocks, and the gradually declining trend in the FCC (text chart). 2/

NAB resources are subject to conditions before they can be activated and used to finance Fund lending. 3/ NAB activation requires approval from NAB participants representing an 85 percent majority of total credit arrangements eligible to vote, as well as the approval of the Executive Board. Key parameters to be included in any activation proposal include the size of the activation; proposed activation period (up to 6 months); and the resource mix of quota to NAB in financing new lending arrangements (usually 1:2, or 1:3). The time needed to activate the NAB may take 6 weeks or more (Annex Figure 7C).

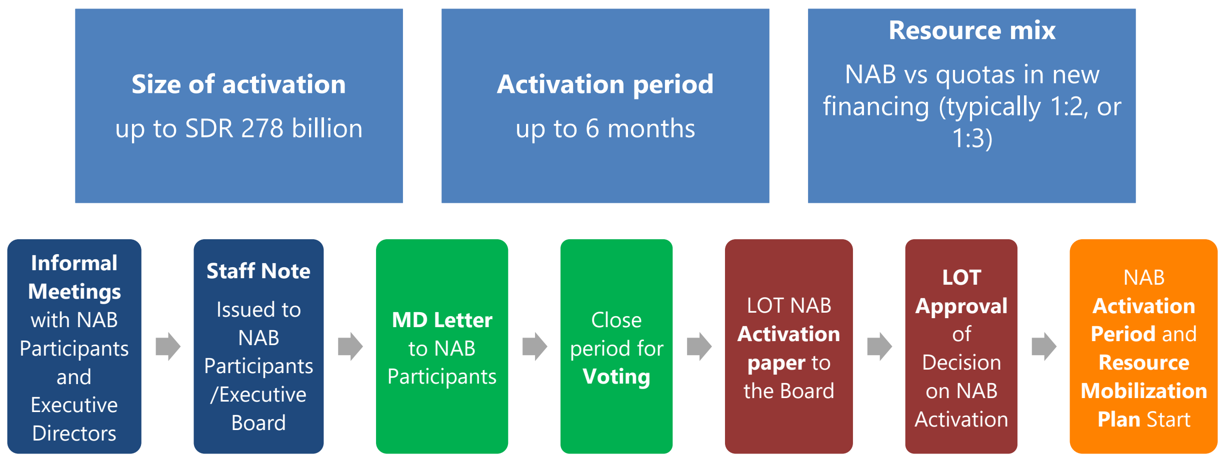
Source: Finance Department; IMF Staff Calculations.

1/ As of end-April 2023.

2/ Previous NAB activations following the global financial crisis, from April 2011 to February 2016, maintained the Fund's liquidity position (modified FCC) at around SDR 250-300 billion.

3/ See the "NAB Decision" (DEC/11428-(97/6), 1/27/1997, as amended, most recently by DEC/16645-(20/5), 1/16/2020).

Annex IX Figure 1.: Key Elements of NAB Activation and Process 1/



In practical terms, the NAB can be activated only when the FCC is expected to fall below SDR 100 billion during an activation period. The NAB decision does not itself specify a threshold for the Managing Director to propose a NAB activation when there may be a case for supplemental resources.[9] However, under U.S. law since 2016, the U.S. can support a NAB activation proposal only if the FCC excluding borrowed resources is expected to fall below SDR 100 billion during the proposed activation period. Given the required 85 percent majority in support of a NAB activation proposal and the U.S.'s share in excess of 15 percent of total NAB credit arrangements, this U.S. requirement effectively sets a threshold for any NAB activation proposal.

NAB resources can only be used to finance commitments made during the NAB activation period. The NAB cannot be used to finance commitments approved before the NAB was activated—these commitments must be financed from quota resources.

- In principle, this constraint could be eased if the current NAB Decision were amended to allow the NAB to finance commitments approved when the NAB was not activated. However, such an amendment would require strong consensus (at least 85 percent support from NAB participants).[10]
- Given the threshold for proposing a NAB activation and since the NAB can finance only GRA commitments when the NAB was activated, the FCC would become a misleading indicator of the Fund's ability to commit new resources under partial scoring. Moreover, if a NAB activation were to be delayed because the FCC remained high under partial scoring, the impact on quota resources would be long-lasting rather than transitory, i.e. the Fund would need to finance more of its lending through quota-only resources prior to the activation of borrowed resources. Nevertheless, creditors could still require the Fund to retain quota resources to co-finance borrowed resources when the latter are eventually activated. Yet if quota resources were to be depleted, this could unduly constrain access to borrowed resources.

[9] Since 2021, however, the NAB decision includes a clause limiting the Fund's ability to seek activation of the 2020 BBAs, linked to the outlook for the modified FCC (paragraph 21). In particular, the Fund may only seek activation of bilateral borrowing during this period where the modified FCC (including all available uncommitted NAB resources) is below SDR 100 billion.

Annex IX Figure 1: Key Elements of NAB Activation and Process (concluded)

Similar constraints apply under the Fund's bilateral borrowing agreements (BBAs). The BBAs are a third line of defense after quotas and NAB and can be activated only if the NAB is also activated or otherwise exhausted. As with the NAB, the BBAs can be used to finance only those lending commitments made during a BBA activation period. Moreover, the *Guidelines for Borrowing* and each individual BBA provides that the BBAs can only be activated if the FCC threshold, as defined under the current FCC Decision[11]—falls below SDR 100 billion.

1/ Upper part covers the key elements of NAB activation, while the lower part refers to the process.

Illustrative Scenarios of Partial Scoring

10. The impact of partial scoring on NAB activation and the Fund's liquidity, compared with full scoring, is illustrated in Table 6. The analysis first presents the data and assumptions underlying the scenarios and then discusses the implications of scoring on Fund's liquidity. Full scoring, the current practice, is considered under two scenarios: (i) the first based on existing precautionary commitments (column 1) and (ii) the second based on hypothetical new demand ("new commitments") for new precautionary arrangements (column 2). Partial scoring is analyzed under three scenarios: (i) the first based on existing precautionary commitments (column 3); (ii) the second based on hypothetical new demand ("new commitments") for new arrangements (column 4); and (iii) third based on additional hypothetical new demand (stress scenario, "additional new commitments") for precautionary arrangements (column 5).

[10] See the "NAB Decision" (DEC/11428-(97/6), 1/27/1997, as amended, most recently by DEC/16645-(20/5), 1/16/2020).

[11] Decision No. 14906 (11/38), adopted April 20, 2011.

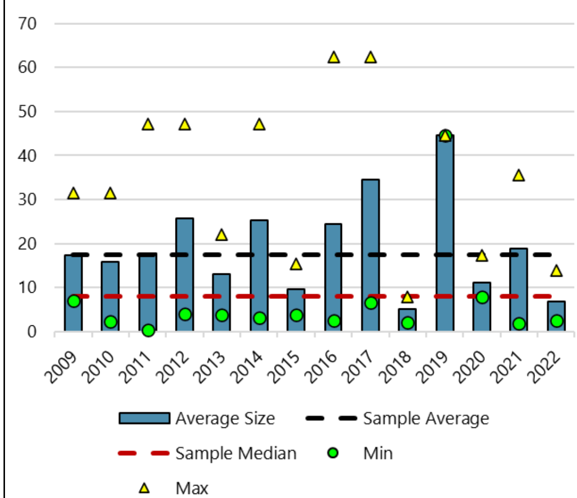
a) Data and assumptions

1. **FCC** *measures the level of resources available for new financial commitments over the next 12 months*. The analysis uses, as the starting point, the actual end-April 2023 FCC of SDR 146 billion and compares the FCC with the threshold of SDR 100 billion for a potential NAB activation (see Annex Box 2).

2. **Available quota liquidity**. This concept, distinct from the FCC, measures the *actual level of quota-based resources immediately available for new financing*, after fully accounting for all existing commitments, but—in contrast to the FCC—excluding future repurchases expected over the next 12 months. [12]

3. **Scoring**. Under the current practice of *full scoring*, both existing and new commitments on a precautionary basis (FCL/PLL/SLL/SBA) are fully reflected (fully counted or scored) in the FCC.[13] The *partial scoring* scenarios assume an illustrative 50 percent partial scoring, implying that commitments on a precautionary basis would be counted in the FCC at half their amounts.

Annex IX Figure 2. Approved Access Under Precautionary Arrangements (in billion SDR) 1/



1/ Includes FCL, PLL/PCL, and SLL arrangements approved since 2009. "Average size" refers to average access for precautionary arrangements approved in a particular year; "max" and "min" refer to individual arrangements approved in a particular year; "sample average" refers to the average over 2009–22.

4. **Demand scenarios**. The following scenarios of demand for precautionary facilities are used: (a) "*existing commitments*" scenario assumes that the current demand for precautionary arrangements will remain unchanged. Two hypothetical new-demand scenarios are also used: (b) "*new commitments*" scenario assumes demand for 4 new precautionary arrangements (for simplicity, under the FCL)—of SDR 20 billion each, broadly in line with the historical access pattern (see text figure)—for a total of SDR 80 billion; and (c) "*additional new commitments*" represents a stress scenario with 3 additional new precautionary arrangements also of SDR 20 billion each, bringing total new demand to SDR 140 billion.

[12] Under full scoring, available liquidity is equal to the FCC excluding scheduled repurchases and repayments of borrowing due in the next 12 months. Prudential balances are not counted under available liquidity as these amounts underpin the encashability of quota resources that is needed to ensure the reserve asset nature of members' claims on the Fund.

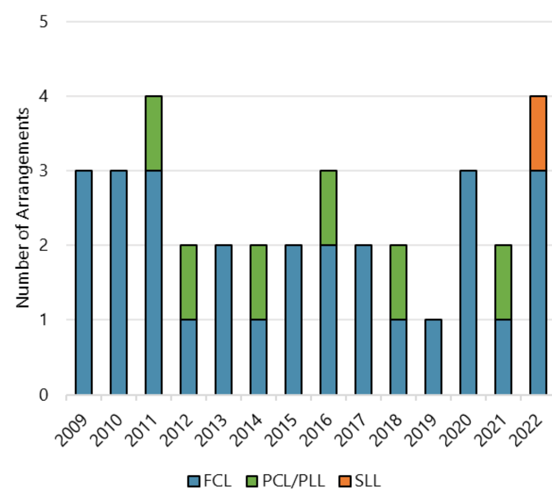
[13] Commitments under current SBAs treated as precautionary are relatively small at SDR 0.3 billion.

5. **Financing mix**. The scenarios assume that new precautionary arrangements are co-financed by quota and borrowing in the ratio of 1:3—in line with past practice. This implies that the Fund would need to preserve about SDR 129 billion of its quota resources for co-financing of NAB and BBAs to be able to deploy its full lending capacity:

- For the NAB alone, in order to access the maximum amount available (SDR 278 billion) if activated, the Fund would need to preserve about SDR 92 billion (i.e. one-third of NAB total) of its quota resources for co-financing.

- Additional quota resources would also need to be preserved in order to co-finance BBAs, which could be activated if available uncommitted NAB resources were to run low, that is, "FCC including NAB resources, is below SDR 100 billion." In this context, this would require preserving additional quota resources in the amount of SDR 36 billion, to access the maximum amount of SDR 108 billion available under BBAs.

Annex IX Figure 3. Frequency of Approved Precautionary Arrangements 1/



1/ Includes FCL, PLL/PCL, and SLL arrangements approved since 2009.

b) Scenario implications

Full Scoring Scenarios

i. **Existing precautionary commitments (column 1).**

Under the current practice, the full amount of existing precautionary commitments—SDR 66 billion as of end-April—is reflected, resulting in the FCC of SDR 146 billion (**row G)**. To meet creditor conditions to activate the NAB, the FCC would need to be projected to fall below the threshold of SDR 100 billion, and this would require new commitments of at least SDR 46 billion. The available quota liquidity (**row I**; see definition above) amounts to SDR 124 billion, which would be immediately available to finance further new commitments of about SDR 124 billion—whether on a drawing or precautionary basis.

ii. **New precautionary commitments (column 2**).

With the approval of 4 new precautionary arrangements of SDR 80 billion in total, the FCC excluding borrowing would fall from SDR 146 to 66 billion, reflecting the full scoring of these new commitments. NAB activation would be possible under this scenario as the FCC would otherwise fall below the SDR 100 billion threshold. NAB resources could then be used to co-finance the 4 new arrangements (at 1:3 ratio), for which the Fund would have sufficient quota resources remaining. However, the calculations of the FCC and available liquidity in this scenario do not make assumptions about the size of the potential NAB activation, and thus in reality both concepts would be higher than the values in column 2.

Partial Scoring (50 Percent) Scenarios

i. **Existing precautionary commitments (column 3)**

- With partial scoring of 50 percent, existing precautionary commitments of SDR 66 billion are scored at SDR 33 billion, which implies a higher FCC of SDR 179 billion (row G), while the Fund's actual available liquidity to immediately finance new commitments would remain unchanged compared to a fully scored approach in column 1 at SDR 124 billion (row I). Thus, ***partial scoring of precautionary commitments raises the FCC, but does not change the true amount of resources available for lending***.

ii. **New precautionary commitments (column 4)**.

- Upon approval, the 4 new precautionary commitments (SDR 80 billion in total) would be scored at SDR 40 billion; the FCC would fall to SDR 139 billion instead of SDR 66 billion under the current practice of full scoring (**column 2**) implying the NAB could not be activated. But the Fund's actual available liquidity would be dangerously low at SDR 44 billion.

- The consequence of partial scoring is that any requests to draw down the new precautionary arrangements—including in the event of a common shock where borrowers draw down in full—would need to be fully financed from quota resources. Thus, ***partial scoring delays NAB activation, and more quota resources are used.***

- The low level of remaining quota resources (available liquidity) would constrain the Fund's ability to co-finance a subsequent activation of NAB and/or BBA resources, including in the event of rising demand for non-precautionary arrangements as seen in scenario iii below (**column 5)**.

- As long as the Fund is required to use quota resources to co-finance its borrowed resources, partial scoring creates a risk the Fund would have effective access to only a fraction of the borrowed resources. This would imply de facto a reduction in the Fund's total lending capacity (from the current US$936 billion), and potentially undermine the role of the Fund in the GFSN.

iii. **Additional new commitments (stress scenario) (column 5).**

- With approval of 3 additional commitments bringing the total to SDR 140 billion, 50 percent partial scoring would account these at SDR 70 billion. This would bring the

FCC down by a further SDR 30 billion from SDR 139 billion in column 4, to SDR 109 billion. The FCC would still remain above the threshold for a possible NAB activation (SDR 100 billion). However, actual available liquidity would have now turned negative (**row l**).

- In this scenario, ***the Fund would have over-committed its quota resources available to meet potential drawings under its existing precautionary commitments, but would remain unable to access NAB resources*** to finance new lending commitments.

- In the event of a common shock where FCL users simultaneously draw on their commitments, the Fund may not be able to honor its assurances to all FCL arrangement-holders amid a crisis, which could be destabilizing and damage the Fund's reputation and role in the GFSN.

11. In sum, under partial scoring, NAB activation could be delayed and the Fund could potentially commit all its available quota resources, even with the FCC remaining above the NAB activation threshold—effectively restricting access to borrowed resources. With partial scoring the FCC would become a misleading indicator of the Fund's capacity to make new commitments. In a stress scenario, the Fund's liquidity may not be sufficient to honor requests for purchases under already committed financing.

Assessment

12. Full scoring of precautionary arrangements under the FCC remains appropriate in view of the Fund's mandate and financing structure. Key considerations remain: (i) the importance of avoiding any doubts over the Fund's ability to meet its financial commitments under precautionary arrangements and thus ensure their effectiveness as part of the GFSN; (ii) the potential for drawings to be highly correlated in response to external shocks that affect several members at the same time; (iii) partial scoring could undermine the Fund's activation of borrowed resources under existing frameworks; (iv) potentially lead to situations where the Fund would overcommit all of its resources, undermining Fund's role as the "lender of last resort"; and (v) the continued absence under the current framework of an alternative source of liquidity that could be tapped in the event of correlated drawings.

Annex IX Table1. Fund Liquidity under Illustrative Scenarios of Scoring of Precautionary Commitments 1/
(In billions of SDRs)

	100% scoring of precautionary arrangements (current practice)		50% percent scoring for precautionary arrangements		
	Under existing commitments 1	Under new commitments 2	Under existing commitments 3	Under new commitments 4	Under additional new commitments 5
A. Usable Resources 2/	299	299	299	299	299
B. Undrawn GRA commitments (scored)	97	177	65	105	135
Current precautionary 3/	66	66	33	33	33
Current non-precautionary	32	32	32	32	32
Illustrative new precautionary		**80**		**40**	**70**
C. Uncommitted usable resources (A-B)	201	121	234	194	164
D. Repurchases, one-year forward	23	23	23	23	23
E. Repayments of borrowed resources, one-year forward	1	1	1	1	1
F. Prudential Balance (F) 4/	77	77	77	77	77
G. FCC (current definition) (C+D-E-F)	146	66	179	139	109
NAB Activation	No	Yes	No	No	No
H. Actual commitments 5/	**97**	**177**	**97**	**177**	**237**
Current precautionary 3/	66	66	66	66	66
Current non-precautionary	32	32	32	32	32
Illustrative new precautionary		**80**		**80**	**140**
I. Available liquidity (A-F-H) 6/	**124**	**44**	**124**	**44**	**-16**

Source: Finance Department; IMF staff calculations.

1/ Data as of April 30, 2023.

2/ Usable resources (quota-based) consist of (i) holdings of the currencies of members considered by the Executive Board to have a sufficiently strong balance of payments and reserve position for these members currencies to be used in the financing of IMF transactions, and (ii) holdings of SDRs.

3/ Undrawn balances under existing GRA arrangements treated as precautionary, excluding NAB-financed portion.

4/ For quota resources, this represents 20 percent of the quotas of members participating in the Financial Transactions Plan (FTP) and preserves the reserve asset nature of members' claims on the Fund. A 20 percent prudential balance also applies to amounts activated under NAB and BBAs.

5/ This includes the actual level of precautionary lending commitments that the Fund is obliged to make available from quota resources upon request, as well as non-precautionary commitments.

6/ Available liquidity reflects the actual availability of quota-based resources for new loan commitments in case of full drawing on precautionary arrangements and excluding future repurchases. Excludes borrowing as NAB is currently not activated. NAB activation would be possible only under column 2, for which the value of FCC and available liquidity in this scenario are net of any NAB activation.

Annex X. Document Risk Self-Assessment (DRSA)

	Rank	Risk Name	Risk Description
Top Risks to the Fund **WITHOUT** this policy proposal or strategy paper in place	#1	Business: Adapting to changing needs of members	[Status quo] Impact on members if precautionary tools and their cost do not reflect changing needs and the Fund does not provide enough insurance; disengagement of members who feel the Fund does not serve their needs. This risk is mitigated by recent temporary changes in access limits for Fund programs and continuous reassessment/monitoring of the adequacy of the lending toolkit.
	#2	Business: Member engagement	[Status quo] If the Fund fails to provide adequate insurance through precautionary instruments, members could increase their reliance on other layers of the GFSN, e.g. self-insurance and swap lines. At the margin, adds to longer-term risks of fragmentation of the global economy. Heavy reliance on reserves accumulation would also lead to larger global imbalances and slower global economic growth. The same mitigating factors as for Risk #1 apply here as well.
	#3	Reputational	[Status quo] The Fund could be perceived as lacking alignment with its members' needs, potentially eroding trust in the institution's effectiveness and members' willingness to engage.
	#4	*Financial: Adequacy and liquidity of GRA lending resources*	*[Considered but not proposed] A shift to partial scoring would delay and complicate the Fund's access to borrowed resources*
	#6	*Financial: Fund income*	*[Considered but not proposed] A reduction in commitment fees (to incentivize take-up of precautionary instruments) would reduce Fund income*

	Rank	Risk Name	Risk Description
Top Risks to the Fund **WITH** this policy proposal or strategy paper in place	#1	Financial: Credit	Increasing PLL and SLL access limits, allowing for no-exit expectations for low-access precautionary FCL arrangements, explicitly permitting concurrent SLL/FCL use, and/or modifying PLL debt sustainability (DSA) requirements could lead to higher Fund credit risk. Mitigated by: access limits anchored to exceptional access thresholds; retaining FCL exit expectation if access is above 200 percent of quota; the limited technical change to the DSA requirement; continuing qualification requirements that make precautionary instruments accessible only to members with sound/very strong fundamentals and institutional policy frameworks; standard safeguards for access to Fund resources, including debt sustainability and capacity to repay assessments.
	#2	Financial: Adequacy and liquidity of GRA lending resources	Significantly higher demand for precautionary lending reduces the Fund's liquidity and commits a high share of lending capacity. Could potentially require activation of borrowed resources (depending on other Fund lending). Mitigated by review clause--new review of precautionary arrangements if precautionary credit and commitments reaches SDR 150 billion (from current SDR 72 billion)--as well as same factors as those mitigating credit risk.
	#3	Business: traction of advice	If higher take-up of FCL/SLL/PLL arrangements is perceived as loosening lending standards, members may perceive they can qualify with weaker policies, and the Fund's policy advice could have weaker traction. Mitigated by qualification requirements at time of request and subsequent review.
	#4	Operational: process	Concurrent use of FCL and (revolving) SLL instruments, with different repurchase periods, could be operationally challenging