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IMMEDIATE ATTENTION

SM/08/255
Supplement 2

September 8, 2008

To: Members of the Executive Board

From: The Secretary

Subject: **Proposed Reforms to the Exogenous Shocks Facility—Background Information on Financing of PRGF-ESF Operations**

Attached for the **information** of Executive Directors is a supplement to the paper on the Exogenous Shocks Facility (ESF)—background information on financing of PRGF-ESF operations (SM/08/255, 7/28/08).

It is not intended that this paper will be published on the Fund's external website.

Questions may be referred to Ms. Sahay (ext. 37181) and Mr. Lin (ext. 37299) in FIN.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

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INTERNATIONAL MONETARY FUND

Proposed Reforms to the Exogenous Shocks Facility (ESF)—Background Information on Financing of PRGF-ESF Operations

Prepared by the Finance Department

(In consultation with the Legal and Strategy, Policy, and Review Departments)

Approved by Andrew Tweedie

September 8, 2008

1. In response to a request by Executive Directors, this supplement provides additional background information on the availability of resources for the modified ESF, as discussed in SM/08/255.

Availability of PRGF-ESF Resources [1]

2. **As of end-July 2008, available PRGF-ESF loan resources committed by bilateral lenders stood at SDR 2.7 billion.** This includes a new loan of US$1 billion (SDR 0.6 billion) committed by France in the context of the ESF. Available subsidy resources for PRGF-ESF lending are estimated at SDR 1.4 billion in end-June 2008 NPV terms. This reflects actual balances held in the PRGF-ESF and PRGF-HIPC Trusts and subsidy contributions that have been committed but not yet received. It includes subsidy contributions of SDR 218 million pledged by 11 members in the context of the original fund-raising for the ESF, of which SDR 66 million has been received. This compares with the initial target for ESF subsidy resources of SDR 500 million.[2]

Potential Demand for PRGF-ESF Resources

3. **Staff periodically updates its projections of demand for PRGF arrangements on a country-by-country basis, as reported in the regular update papers on concessional financing**. The latest projections suggest that demand could amount to about SDR 1.7 billion over the next two to three years, comprising SDR 0.5 billion in the remainder of 2008 and

[1] See details in the forthcoming semi-annual *Update on the Financing of the Fund's Concessional Assistance and Debt Relief to Low-Income Member Countries*.

[2] See *Establishment of an Exogenous Shocks Facility under the Poverty Reduction and Growth Facility Trust* (SM/05/365, 10/4/05).

SDR 1.2 billion in 2009–10.[3] This would imply a significant pick-up in demand compared with the last four years (2004–07) when demand for PRGF loan resources averaged SDR 0.3 billion a year. Actual demand over this period has consistently fallen short of projections.[4]

4. **Staff has not made detailed projections of demand under the modified ESF.** As noted in SM/08/255, this demand is difficult to project, as the facility is designed to help countries deal with exogenous shocks that, by definition, are hard to forecast.[5] Two scenarios were illustrated in SM/08/255 based on mechanical assumptions of demand by a broad range of countries. Staff has also considered a third scenario focusing on those countries with relatively weak balance of payments positions.[6] If augmentation of 15 percent of quota (the average of the recent cases) were requested under PRGF arrangements[7] and all remaining PRGF-eligible countries with relatively weak external reserves positions requested rapid access of 25 percent of quota under the ESF, total new lending would amount to SDR 1.3 billion.

5. **Of the available subsidy resources of SDR 1.4 billion, SDR 0.6 billion would be required to cover existing PRGF arrangements**. This would leave a balance of SDR 0.8 billion that could subsidize new PRGF-ESF loans of about SDR 3.2 billion (based on current estimates, some additional loan resources would be needed to fully utilize existing subsidies). This appears adequate to accommodate a significant pick-up in demand under the PRGF-ESF over the next 2–3 years. For example, if demand under the PRGF is in line with current projections of SDR 1.7 billion as noted above, this would still leave roughly SDR 1.5 billion for potential demand for shocks financing.

Implications of Strong Demand under the Modified ESF

6. **If demand for the modified ESF turns out to be very strong, and higher than what can be accommodated by the remaining subsidy resources, the following options would be available.** One would be to complete the original fund-raising exercise for the ESF

[3] These projections exclude the remaining protracted arrears cases of Somalia, Sudan, and Zimbabwe. Zimbabwe has protracted arrears to the PRGF-ESF Trust and was removed from the list of PRGF-eligible countries by Executive Board Decision No. 12582-(01/99), adopted September 24, 2001.

[4] In 2008 to date, demand has amounted to SDR 0.6 billion.

[5] When the ESF was originally introduced, potential demand was estimated at SDR 2 billion over five years, but actual demand has so far been zero.

[6] Countries with external reserve coverage of less than three months of imports. See *Food and Fuel Prices—Recent Developments, Macroeconomic Impact, and Policy Responses* (SM/08/182, 6/19/08).

[7] Excluding those that have already received augmentation in the context of the current food and fuel price shock.

by seeking additional resources in line with the request for subsidy resources to cover ESF operations for the first five years of SDR 500 million. A second option, as discussed in SM/08/255, would be to advance the date for initiating the self-sustained PRGF-ESF operation. This would have some impact on the Fund's future concessional lending capacity as noted in FO/DIS/08/23 (a one-year change in the start date of the self-sustained PRGF-ESF operation is estimated to have an impact on the concessional lending capacity of about SDR 45 million per annum).