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## **IMF Overhauls Lending Framework**

The Executive Board of the International Monetary Fund (IMF) today approved a major overhaul of the IMF's lending framework, including the creation of a new Flexible Credit Line (FCL).

"These reforms represent a significant change in the way the Fund can help its member countries—which is especially needed at this time of global crisis," said IMF Managing Director Dominique Strauss-Kahn. "More flexibility in our lending along with streamlined conditionality will help us respond effectively to the various needs of members. This, in turn, will help them to weather the crisis and return to sustainable growth."

Mr. Strauss-Kahn invited strong-performing countries that may be hit by the global crisis to use the new Flexible Credit Line which he said "could strengthen further their economic position."

The changes to the IMF's lending framework include:

- modernizing IMF conditionality for all borrowers,
- introducing a new Flexible Credit Line,
- enhancing the flexibility of the Fund's traditional stand-by arrangement,
- doubling normal access limits for nonconcessional resources,
- simplifying cost and maturity structures, and
- eliminating certain seldom-used facilities.

Reforms of concessional lending instruments for low-income members are also in train. In addition, the IMF is consulting with its members to secure a sharp increase in its lending resources.

"Today's action represents an important evolution in the Fund's lending framework," said Mr. John Lipsky, First Deputy Managing Director. "We arrived at these reforms by listening to our membership, consulting with a variety of stakeholders, and reviewing past experiences. These reforms will pave the way for countries to work more effectively with the Fund on crisis prevention and crisis resolution."

## ANNEX

**IMF IMPLEMENTS MAJOR LENDING POLICY IMPROVEMENTS**

In response to the deepening global economic difficulties, the IMF is implementing a series of reforms that will strengthen its lending framework. These measures reflect consultations with Fund members and stakeholders, and will enable the Fund to respond more effectively to the evolving challenges of crisis-affected countries.

Emerging market and developing countries are facing increasing strains from the global economic downturn. As the crisis is becoming more prolonged, many of these countries are finding that their room for policy maneuver is becoming more constrained. In these circumstances, timely IMF financing—if provided in an appropriate amount and form—can cushion the economic and social costs of external shocks. In some cases Fund assistance could help prevent crises altogether.

Against this background, the **IMF Board has approved a major overhaul to the Fund's lending framework** by:

- modernizing IMF conditionality,
- introducing a new flexible credit line,
- enhancing the flexibility of the Fund's regular stand-by lending arrangement,
- doubling access limits,
- adapting and simplifying cost and maturity structures for its lending, and
- eliminating facilities that were seldom used.

In addition, the IMF is seeking to sharply increase both its nonconcessional and concessional lending resources, which would enable it to meet expanded financing requirements in the crisis. Reforms of concessional lending instruments for low-income members are also in train.

***Modernizing conditionality.*** The IMF aims to ensure that conditions linked to IMF loan disbursements are focused and adequately tailored to the varying strengths of countries' policies and fundamentals. In the past, IMF loans often had too many conditions that were insufficiently focused on core objectives.

This modernization is to be achieved in two key ways. First the IMF will rely more on pre-set qualification criteria (ex-ante conditionality) where appropriate rather than on traditional (ex post) conditionality as the basis for providing countries access to Fund resources. This principle is embodied in a new Flexible Credit Line. Second, implementation of structural policies in IMF-supported programs will from now on be monitored in the context of program reviews, rather than through the use of structural performance criteria, which will be discontinued in all Fund arrangements, including those with low-income countries. While structural reforms will continue to be integral to Fund-supported programs where needed,

their monitoring will be done in a way that reduces stigma, as countries will no longer need formal waivers if they fail to meet a structural reform by a particular date.

***Flexible Credit Line*** (FCL). The IMF is introducing a new credit line for countries with very strong fundamentals, policies, and track records of policy implementation. Access to the FCL credit line will be particularly useful for crisis prevention purposes. FCL arrangements would be approved for countries meeting pre-set qualification criteria. Access under the FCL would be determined on a case-by-case basis. Disbursements under the FCL would not be phased or conditioned to policy understandings as is the case under a traditional Fund-supported program. This flexible access is justified by the very strong track records of countries that qualify for the FCL, which give confidence that their economic policies will remain strong.

The terms of the FCL represent a strengthening of the earlier Short-Term Liquidity Facility (SLF), which therefore will be discontinued. While the SLF was also designed to cater only to very strong-performing members, several of its design features—including its capped access and short repayment period, as well as the inability to use it on a precautionary basis—limited its usefulness to potential borrowers. The concept of a credit line available for either crisis prevention or resolution and dedicated for only very strong-performing countries, with all its flexible features is new.

The FCL's flexibility includes:

- Assuring qualified countries of large and upfront access to Fund resources with no ongoing (ex post) conditions;
- Renewable credit line, which at the country's discretion could initially be for either a six-month period, or a 12-month period with a review of eligibility after six months;
- Longer repayment period (3¼ to 5 years versus maximum rollover period of 9 months in the SLF);
- No hard cap on access to Fund resources, which will be assessed on a case-by-case basis (the SLF had a cap on access of 500 percent of quota); and
- Flexibility to draw at any time on the credit line or to treat it as a precautionary instrument (which was not allowed under the SLF).

The pre-set qualification criteria are at the core of the FCL and serve to signal the Fund's confidence in the qualifying member's policies and ability to take corrective measures when needed. At the heart of the qualification process is an assessment that the member (a) has very strong economic fundamentals and institutional policy frameworks; (b) is implementing—and has a sustained track record of implementing—very strong policies, and (c) remains committed to maintaining such policies in the future. The relevant criteria for the purposes of assessing qualification for an FCL arrangement include: (i) a sustainable external position; (ii) a capital account position dominated by private flows; (iii) a track record of steady sovereign access to international capital markets at favorable terms; (iv) a reserve position that is relatively comfortable when the FCL is requested on a precautionary basis; (v) sound public finances, including a sustainable public debt position; (vi) low and stable

inflation, in the context of a sound monetary and exchange rate policy framework; (vii) the absence of bank solvency problems that pose an immediate threat of a systemic banking crisis; (viii) effective financial sector supervision; and (ix) data transparency and integrity. Strong performance against all these criteria would not be necessary to secure qualification under the FCL, as compensating factors, including corrective policy measures under way, would be taken into account in the qualification process.

***Enhancing Stand-by Arrangements (SBA).*** Reforms to the SBA—the Fund’s workhorse lending instrument for crisis resolution—aim to increase its flexibility and ensure its availability as a crisis prevention instrument for members that may not qualify for the FCL. The new SBA framework will enable high-access on a precautionary basis and provide increased flexibility by allowing frontloading of access and reducing the frequency of reviews and purchases where warranted by the strength of the country’s policies and the nature of the balance of payments problem faced by the country.

***Doubling access limits.*** Nonconcessional loan access limits for countries are being doubled, with the new annual and cumulative access limits for Fund resources being 200 and 600 percent of quota, respectively. These higher limits aim to give confidence to countries that adequate resources would be accessible to them to meet their financing needs. Access above these limits will continue to be provided on a case-by-case basis under Exceptional Access procedures, which are also being clarified and streamlined.

***Adapting and simplifying cost and maturity structures.*** To create the right incentives for borrowing from the Fund, the cost and maturity structures for high-access and precautionary Fund lending are also being overhauled. The elimination of the time-based repurchase expectations policy—an administrative mechanism meant to induce early repayments—will effectively lengthen grace periods and simplify the repayment schedules of Fund lending. This administrative mechanism is replaced by the introduction of a new time-based surcharge, which together with streamlined level-based surcharges, will help mitigate credit risks without increasing the cost of borrowing to countries that make timely repayments to the Fund. The new schedule of commitment fees, which increases with the size of precautionary lending, would help mitigate liquidity risks to the Fund without discouraging early access to IMF resources.

***Reform of facilities for low-income country members.*** In addition to the reform of structural conditionality, which applies also to concessional loan facilities available for low-income countries, the Fund is considering modifications to its concessional lending facilities to strengthen the IMF’s lending tools for providing short-term and emergency financing to low income countries.

***Simplifying lending toolkit.*** Some facilities that have not been recently used (Supplemental Reserve Facility and the Compensatory Financing Facility) are being eliminated.

***Boosting the Fund’s resources.*** A substantial increase in the IMF’s resources is required to give full confidence to countries that the Fund will have sufficient money available should they need to borrow. Japan has already provided the IMF with an additional US\$100 billion to bolster the Fund’s lendable resources available to address the current crisis to about

US\$350 billion, and the European Union has committed €75 billion. Efforts are under way to further increase IMF resources in the run-up to the April 2 London summit of the G-20, and to at least double concessional resources for low-income countries.