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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 09/40-2

10:19 a.m., April 21, 2009

2. Financing the Fund's Concessional Lending to Low-Income Countries—Resource Needs and Options

Documents: SM/09/94

Staff: Tweedie, FIN; Hagan, LEG

Length: 1 hour, 52 minutes

Executive Board Attendance

D. Strauss-Kahn, Chairman

Executive Directors	Alternate Executive Directors
S. Itam (AE)	M. Majoro (AE)
L. Rutayisire (AF)	K. Assimaidou (AF)
	V. De la Barra (AG), Temporary
	C. Legg (AU)
W. Kiekens (BE)	
P. Nogueira Batista, Jr. (BR)	
	J. He (CC)
	J. Cova (CE), Temporary
	S. Ladd (CO), Temporary
A. Fayolle (FF)	B. Claveranne (FF)
K. Stein (GR)	
	N. Choudhary (IN), Temporary
A. Sadun (IT)	
D. Kotegawa (JA)	
J. Mojarrad (MD)	
	S. El-Khouri (MI)
	W. Schilperoort (NE), Temporary
	J. Bergo (NO)
	A. Lushin (RU)
	A. Al Nassar (SA)
	A. Chua (ST)
T. Moser (SZ)	
M. Lundsager (UA)	D. Heath (UA)
A. Gibbs (UK)	J. Talbot (UK)

G. R. Kincaid, Acting Secretary
R. Mowatt, Assistant

Also Present

African Department: R. Nord, A. Sayeh. Asia and Pacific Department: T. Rumbaugh. External Relations Department: I. Dieng, T. McAnthony, M. Schindler. Finance Department: D. Andrews, M. Fisher, E. Goirand, G. Kabwe, J. Lin, P. Njoroge, R. Price, J. Ralyea, T. Redfern, Y. Sun-wang, A. Tweedie. Legal Department: K. Christopherson, S. Hagan, I. Mouysset, B. Steinki, R. Weeks-Brown. Office of the Managing Director: D. Citrin, C. McDonald, R. Rosales. Secretary's Department: P. Gotur, P. Martin, P. Ramlogan. Strategy, Policy, and Review Department: H. Bredenkamp, D. Desruelle, S. Fabrizio, E. Gemayel, J.K. Martijn, I. Mateos y Lago, R. Moghadam, C. Mumssen, Y. Yang. Western Hemisphere Department: P. Alonso-Gamo, C. Macario. Senior Advisors to Executive Directors: W. Abdelati (MI), C.Dahlhaus (GR), H. Djoufelkit (FF), A. Joseph (BR), M. Kaplan (UA), D. Kihara (JA), M. Morgan (CO),

A. Ndyeshobola (AE), S. Rouai (MD), D. Sembene (AF), R. Weber (SZ). Advisors to Executive Directors: T. Galac (NE), R. Hills (UK), G. Jung (SZ), R. Lin (CC), C. Mira (CE), K. Mogensen (NO), S. Rottier (BE), Y. Shinagawa (JA), D. Tartari (SZ), G. Tesfamichael (AE), N. Thapa (ST), C. Thompson (AU), J. Thornton (UK), E. Uanguta (AE), F. Valeri (IT).

2. FINANCING THE FUND'S CONCESSIONAL LENDING TO LOW-INCOME COUNTRIES—RESOURCE NEEDS AND OPTIONS

Mr. Kiekens submitted the following statement:

To enable the PRGF-ESF Trust to lend SDR 2 billion per year over the next two years, and about SDR 1.5 billion per year thereafter until 2015, the Trust would need additional loan resources of SDR 9 billion and subsidy resources of SDR 1.5 billion. The staff assumes it will be possible for the Trust to borrow the needed principal. To cover the needed SDR 1.5 billion subsidy resources, the staff submits, for consideration of the Board, four options:

Transfer of SDR 0.74 billion from the PRGF-ESF Reserve Account to the PRGF-ESF Subsidy Account

The resources in the reserve account are scheduled to be used for the so-called "self-sustained" PRGF-ESF operations, once the existing subsidy resources are depleted after 2015. These self-sustained operations could amount to about SDR 0.7 billion annually.

The staff now estimates that transferring SDR 0.74 billion from the reserve account to the subsidy account would still allow the balance of the reserve account to finance loans in the order of SDR 0.7 billion annually from 2015 onwards.

This proposal looks sensible. However, before accepting it, we would like to request staff to clarify its calculations by updating FO/DIS/08/23, in particular by using lower market interest rates and a lower margin than the 90 basis points premium return on investments, assumed last year.

Delaying the Reimbursement to the GRA of its Administrative Expenses related to the PRGF-ESF Trust

The reimbursement of the GRA's expenses for administering the PRGF-ESF Trust is an integral and important part of the new income model agreement. We insist that it be adhered to.

The conditions for a temporary suspension of the reimbursement, as contemplated in Decision 14093-(09/32) are not in place. The Fund should, at a minimum, first evaluate the results of efforts to obtain additional subsidy resources from donors.

I observe that the staff evaluates the amount of these administrative costs at about SDR 51 million annually.

For a long time we have insisted that the Fund establishes a transparent cost-accounting framework that would allow to assess with clarity the costs of the different tasks of the Fund staff, including the cost related to PRGF-ESF operations and, of course, the administrative costs related to GRA lending. We invite staff to update the Board on progress in this respect, in time for the April 29, 2009 Board meeting on the Fund's income position.

Even if sufficient bilateral subsidy resources would not be forthcoming, we cannot conclude today that forgoing the reimbursement of the GRA would be the right option. One alternative option would be to evaluate the relative importance of increasing PRGF lending today versus future lending, and whether it would be justifiable, in light of the priorities of donors for their ODA spending, to reduce the capacity of the self-sustained PRGF-ESF after 2015 in favor of a higher lending capacity in the next few years.

Profits from Gold Sales

The staff invites the Board to consider whether it would be consistent with the new income model to commit to pay dividends with the expectation that countries would use these revenues to give sufficient donor contributions to the PRGF-ESF Trust.

I give short shrift to this option. We should not commit paying dividends before sufficient profits are realized.

There is no realistic basis for the assumption that in the next 5 to 7 years, the Fund's income would allow paying dividends.

The income model requires that all the proceeds of gold sales, irrespective of the average sales price, be allocated to an endowment.

We have to wait for a stable long-term pay-out from the gold endowment, and evaluate how much of this pay-out will be in excess of what the Fund needs to cover its administrative expenses not related to lending operations, and to build up prudent reserves not related to credit risk.

As shown in Table 3 of EBS/09/51, the Fund's investment income from reserves is projected to drop from SDR 345 in FY2009 to

SDR 83 million in FY2010 (and beyond), assuming an SDR rate of 0.9 percent. Rather than expecting surplus income, the Fund is likely to be confronted with a significant drop of expected investment income.

It is correct that the Fund is likely to receive additional income from lending operations. However, as the staff rightly points out in paragraph 23, the new income model envisages that the Fund will rely on broader, more sustainable sources of income to finance its diverse activities, rather than rely primarily on lending income. Charges, surcharges and fees for GRA lending should cover only the Fund's intermediation costs and the build-up of precautionary reserves. They are not levied to generate dividends. Moreover, precautionary reserves are seen as still insufficient.

We observe that, in the coming years, the Fund is projected to receive only about SDR 152 million income (of which SDR 51 million reimbursement by the PRGF-ESF Trust) from other sources than lending, greatly insufficient to cover its expenses not related to lending.

In conclusion, under the new income model, member countries should not expect to receive dividend payments from the Fund in the period until 2015.

New Bilateral Contributions

The contributors to the PRGF-ESF Trust are ultimately responsible for deciding the size of the Trust's lending operations.

As a member of the Board of Trustees, I am willing to agree with a responsible increase in loan amounts that will benefit low-income countries. It is up to the Trust contributors to make the necessary resources available.

I support the proposal that the Managing Director calls on member countries to contribute the needed subsidy resources. This should be manageable, as the total subsidy amount of about SDR 750 million, can be paid over the next 7 years. If pledges are credible, payments can be backloaded somewhat if today's difficult budget situation so requires. Even so, increasing ODA today would be a responsible strategy that the Fund and the World Bank must encourage. As President Zoellick has suggested, why not ensure that 0.7 percent of the fiscal stimulus measures takes the form of ODA. In today's integrated world, fiscal stimulus spent abroad is likely to benefit also many partner countries of the donor recipients.

Experience shows that good burden sharing contributes to successful fundraising. I suggest that the Managing Director draws a list of all advanced and resources-rich countries that should be invited to contribute, indicating for each country a range of suggested contributions, based on reasonable transparent parameters.

The Managing Director should invite each country on this list to contribute. We should be transparent on the results of the Fund's efforts to collect the necessary resources to help the countries with the highest needs.

Mr. Gibbs and Mr. Thornton submitted the following statement:

In their Declaration on Delivering Resources through the International Financial Institutions, the G20 leaders declared:

"We have committed, consistent with the new income model, that additional resources from agreed sales of IMF gold will be used, together with surplus income, to provide $6 billion additional concessional and flexible finance for the poorest countries over the next two to three years. "

We feel that the proposals in the staff paper risk falling short of the G20 commitment. The clear implication of the above is that the Fund should resource an additional $6 billion in concessional lending for LICs. Yet the proposals provided in this paper provide a very uncertain and shaky foundation for achieving this commitment. At a time when the IMF's income stream is more assured than ever, this institution's financial security should not and must not come at the expense of the poorest and most vulnerable countries. We need to move forward in a way which protects the income model without putting the G20 commitment at risk.

We agree that the reimbursement of the GRA for PRGF-ESF administrative costs can and should form part of the solution.

We have provided substantial bilateral contributions in the past and certainly encourage others to contribute on a fair burden share basis. Nevertheless, we find the estimate of 0.1 to 0.3 billion SDR in additional contributions to be very optimistic given the extreme fiscal pressure currently faced by donors. In the event that these funds do not materialize, the obligation to fund the concessional financing remains.

Of the options on the use of gold sales, only option 3 appears to be consistent with the commitment to finance the additional $6 billion. Options 1 and 2 could only be considered as part of a fully financed package that made further use of surplus income to fill any gap.

We therefore ask staff to come forward with a concrete proposal which will ensure that the $6 billion is fully financed and not solely reliant on the vagaries of gold prices and uncertain over donor financing.

Mr. Lushin submitted the following statement:

We thank the staff for an informative paper that contains a number of interesting proposals. Before we turn to discussing specific proposals on how to mobilize concessional financing, we think it is necessary to reach a common understanding on what the G-20 Leaders' commitment actually means. It says:

"We have committed, consistent with the new income model, that additional resources from agreed sales of IMF gold will be used, together with surplus income, to provide $6 billion additional concessional and flexible finance for the poorest countries over the next two to three years".

We remain doubtful about how to interpret the first part of this sentence, which mentions additional resources from sales of IMF gold as well as the surplus income. We are unclear about what the word "additional" means in this context, what are the sources of surplus income and the surplus to what it should be. If the word "additional" refers to resources from gold sales above those needed for sustaining the new income model, then it is not clear what the source of any surplus income will be, if this income is expected to appear from investing the proceeds of gold sales. These technical hurdles notwithstanding, the general message is clear – the Fund needs to somehow use its gold to generate concessional financial resources for LICs.

We think we were more successful in understanding the second part of the Leaders' commitment. Again, the key word here is "additional" and it is necessary to clarify additional to what $6 billion should be. The most logical and reasonable understanding, in our view, is that they should be additional to the existing level of the Fund's concessional financing, which we can approximate with an annual average in 2000-2008, equal to SDR 0.7 billion. On the basis of this understanding we can easily calculate the amount of subsidy resources the Fund should generate to accommodate the G-20 commitment. These amounts will be different in "2 years" and "3 years" scenarios, as explained below.

For two years (2009-10), the size of "normal" financing will be 0.7 x 2 = SDR 1.4 billion. To this we should add the G-20 commitment of $6 billion (SDR 4 billion) and get SDR 5.4 billion. The Fund now has subsidy resources that could subsidize new concessional lending of SDR 4.5 billion, which means we need to mobilize extra subsidy resources for additional concessional lending of SDR 0.9 billion (5.4 – 4.5). Given that for every SDR 1 billion of concessional lending about SDR 0.2 billion of subsidy resources is required[1], the "2 years" scenario will need to be supported by additional subsidy resources of SDR 0.18 billion. Assuming a 10 percent leakage from the dividend distribution, the amount of resources that has to be generated by gold will be SDR 0.2 billion, or $0.3 billion.

Similar calculations for a "3 years" scenario (2009-2011) give the required amount of subsidy of SDR 0.32 billion or SDR 0.36 billion ($0.54 billion) if the leakage is taken into account.

All in all, our understanding of the G-20 Leaders' commitment implies the need for the Fund to use $0.3-0.5 billion from its gold sale profits to subsidize concessional lending. This is somewhat lower than the amount proposed by the staff in Option 3 ($0.8-1.0 billion). The difference derives from the fact that in their calculations the staff tries to cover the subsidy needs for the period of 2009-15, which goes well beyond the G-20 requirement, extending only to 2010-2011.

The short-term nature of the G-20 request for additional concessional financing is very understandable – we should considerably increase concessional financing of LICs right now, when these countries are coping with the consequences of the current global crisis. Going forward (and beyond the crisis), the financing needs of LICs are highly uncertain and we have already emphasized during the previous discussion that the staff's estimate for 2011-15 (SDR 7.5 billion) is nothing but a guess subject to a large margin of error. Trying to build our resource mobilization efforts on this shaky foundation would be a mistake, in our view. The Fund (and the international community at large) should return to this issue in one or two years, when the prospective financing needs of LICs become clearer. Apart from having greater certainty, doing this later may also have an advantage of a stronger capacity of donors to contribute as compared with the present-day situation.

[1] Staff says in SM/09/94 that the expected demand for concessional lending of SDR 7.5 billion in 2011-15 requires SDR 1.5 billion of subsidy resources. This gives SDR 0.2 billion of subsidies for every SDR 1 billion of concessional loans (1.5 / 7.5).

The mobilization of the required amount of gold profits ($0.3-0.5 billion) should be implemented quickly, as soon as the Fund gets clearance for gold sales, in order to ensure that these resources are used over the next two to three years, as the G-20 Declaration stipulates. The very first tranche of these sales in (presumably) FY2010 should be used to this end.

Finally, we disagree with the proposal to suspend the reimbursement of the GRA for PRGF-ESF expenses. The decision to resume the reimbursement has been an integral part of the new income model, and this should not be reversed. Non-reimbursing the GRA for PRGF-ESF expenses will prolong the practice of bad financial governance of cross-subsidization of one group of countries at the expense of another group. Moreover, our literal reading of the G-20 Declaration suggests that suspending the reimbursement is not required from the financial standpoint.

Mr. Rutayisire submitted the following statement:

We thank the staff for a well-written paper and welcome the opportunity to discuss the financing of Fund's concessional lending to low-income countries (LICs). As raised in the Board discussion on the Fund's role in LICs, we are of the view that staff's projections of LICs' financing needs occasioned by the current global crisis and related demand for Fund's concessional resources are too conservative and subject to a great deal of uncertainty. Staff has estimated that SDR 9 billion in additional PRGF-ESF loan resources and SDR 1.5 billion in additional PRGF-ESF subsidy resources will be needed to meet projected short and medium-term demand for Fund's concessional lending. Given the uncertainties posed by the global financial crisis, we believe that prudence dictates that the Fund errs on the side of caution by aiming to mobilize more than these amounts. Incidentally, such an approach would be especially opportune, given that an upward shift in trend of SDR interest rates, which is very likely in the near future, would reduce the level of Fund lending that available resources can subsidize.

The Need for Additional Loan and Subsidy Resources

We note staff's assertion that loan resources have traditionally been easier to mobilize, given that the market return earned by lenders is generally linked to the SDR interest rate. At the same time, we understand that this interest rate is currently at a record low, after having sharply declined from more than 4 percent in 2006 to less than 0.5 percent in recent days. Under these circumstances, we are concerned that mobilization of loan resources could not prove more challenging than usual, as lenders may lack market incentives to consider favorably Fund's requests for additional loan resources, given that such loans would potentially generate insignificant market returns, at least in the near term. Staff's comments are welcome.

As suggested by staff, it would be helpful that some member countries would consider lending to the PRGF-ESF Trust part or all of their SDR allocations. In this connection, we call on staff to identify the necessary modalities for lending SDRs to the PRGF-ESF Trust.

The staff paper notes that subsidizing the projected demand for Fund's concessional lending through 2015 will require additional subsidy resources of about SDR 1.5 billion. In our view, all options for financing these subsidy needs should be explored, including proceeds from gold sales, bilateral contributions, and the use of resources from the PRGF-ESF Trust Reserve Account. With regard to the latter, we note staff's view that the allocation of about SDR 0.74 billion from this account to the subsidy account could cover half of the additional subsidy needs through 2015 without undermining the long-term "self-sustained" subsidization capacity of SDR 0.7 billion after 2015. However, we see merit in aiming for a much higher long-term subsidization capacity of the Reserve Account. In present circumstances, given staff's estimate that the use of PRGF-ESF resources would be about SDR 1.5 billion around 2015, achieving a "self-sustained" subsidization capacity of at least this amount would be desirable. For this reason, we believe that drawing from the Reserve Account should be only done at last resort and priority must be given at this stage to other available financing options.

Financing Options

The staff paper presents various options for financing the Fund's needs for additional concessional resources, including bilateral contributions, revenues from gold sales, and delay in the reimbursement of the GRA for PRGF-ESF Trust administrative expenses. While all of these options should be explored for efficiency purposes, priority should be given to more predictable and sustainable sources of financing, given the urgency of the situation.

In our view, the use of part of the proceeds from gold sales remains one of the most promising options for generating sufficient and predictable resources to support Fund's concessional lending. We take note of staff's assertion that the Articles of Agreement allow only for an indirect transfer from gold sales to subsidy account resources by which the proceeds of the gold sales are first distributed to members in proportion to their quotas and then returned as subsidy contributions. The fact that all staff-proposed options for financing Fund's concessional resource needs with part of the proceeds from gold sales involve indirect transfers is a cause for concern about a timely mobilization of such resources. Could staff elaborate on how to guarantee an effective and prompt return of these revenues as subsidy resources? Would it be possible to ensure that the distribution of the proceeds and their return as subsidy resources take effect simultaneously in order to avoid country procedures for returning these resources that could be potentially lengthy and of uncertain outcomes?

In our view, Options 1 and 2 seem unattractive since they cannot guarantee that gold sales will lead to a timely and effective mobilization of the additional resources needed to finance LIC subsidy needs. We have a preference for a financing option along the lines of Option 3 which guarantees the use of a pre-determined amount of gold sale proceeds to finance LIC subsidy needs. As noted in the staff paper, such an option would ensure certainty over the contribution to subsidy resources generated by gold sales. However, we find staff proposed subsidy contributions from gold sales proceeds which are in the range of SDR 0.5-0.6 billion to be overly conservative. We suggest that such contributions be determined to fully cover projected subsidy needs, thereby protecting the PRGF-ESF Trust from potential and likely shortfalls in bilateral contributions and preserving the subsidization capacity of the PRGF-ESF Reserve Account. Staff's comments are welcome.

As noted by staff, expecting bilateral contributions to fully cover the needs for subsidy resources is not realistic in current circumstances. Recent trends in bilateral assistance have been way below expectations in the face of LICs' growing needs for concessional financing. And under current circumstances characterized by an unprecedented global crisis, it does seem reasonable to expect an imminent reversal of these trends. Nonetheless, we concur that a limited fund-raising effort may still be needed and, in this regard, we note staff's plans to mobilize about SDR 0.1-0.3 billion, as part of the resources needed to meet subsidy requirements. Still, we feel that it would be prudent that contingency plans be developed to compensate for potential shortfall in mobilizing this targeted amount.

We fully share staff's view that current circumstances warrant the suspension of the reimbursement of the GRA for PRGF-ESF Trust administrative expenses, consistent with the Board Decision No. 14093-(08/32) which authorizes gold sales. Clearly, it is hard to find credible arguments against the consistency of such a measure with the related Board

Decision, at a time when exactly the topic of the day is about financing additional resources to supplement resources available in the PRGF-ESF Trust to meet the rising demand for Fund's concessional assistance. Indeed, the difficult income situation that led the Fund to take this measure has been made history by the sharp increase in Fund lending over recent months. In addition, the implementation of this measure would be associated with significant adverse effects on the lending capacity of the PRGF-ESF Trust which would largely offset the incremental, additional revenues that it would generate for the GRA.

Rather than just delaying the reimbursement of the GRA for PRGF-ESF Trust administrative expenses, we call for the repeal of the related Board decision. In the event, the Board would instead opt for the suspension of the planned reimbursement of the GRA for PRGF-ESF Trust administrative expenses, we would have a preference for such a suspension to take effect for at least 5 years.

Finally, we would appreciate it if staff could give us, for each possible source of financing, an idea of the proposed timeframe during which the necessary loan and subsidy resources are expected to be mobilized.

Mr. El-Khouri and Ms. Choueiri submitted the following statement:

We thank staff for a concise paper presenting initial considerations for mobilizing the additional subsidy resources needed to support a doubling of the Fund's concessional lending capacity over the medium term. It is important that efforts to secure an expanded resource envelope for concessional financing proceed in tandem with the enactment of the proposals for reform, and we would have preferred that today's discussion had not presumed an outcome on the modification of access policies and norms. We would like to note that the views we express in this statement should be considered as preliminary, since the very short period of circulation for the staff report did not allow us to consult with our authorities on the subject.

The paper seeks to respond to the request by the Leaders of the Group of Twenty that "consistent with the new income model (…) additional resources from agreed sales of IMF gold (…) be used, together with surplus income, to provide $6 billion additional concessional and flexible finance for the poorest countries over the next 2 to 3 years." Staff estimate the associated resources needed to subsidize projected demand for concessional lending through 2015 to amount to about SDR 1.5 billion (end-2008 NPV terms).

Use of the Fund's income to provide the needed subsidy resources as called for by the Group of Twenty would entail committing part of the institution's income to a subset of activities and countries, which might not be the most appropriate course of action from the point of view of the Fund's income and mandate. We have serious reservations on measures such as delaying the reimbursement to the GRA and profits from gold sales, which form an integral and central part of the new income model. Their (partial or total) use in the context of this paper would imply diverting resources away from the Fund's core non-lending activities, namely surveillance and capacity building, as well as the Fund's expanded financial stability role. This could hamper the Fund's capacity to fulfill its mandate effectively, and would therefore be inconsistent with the objectives of the new income model. Notwithstanding these reservations, we will comment in what follows on all the options presented by staff for mobilizing the necessary resources needed to double the Fund's concessional lending capacity.

The PRGF-ESF Trust Reserve Account

Before envisaging financing options, staff suggests tapping the PRGF-ESF Trust Reserve Account for about SDR 0.74 billion to meet part of the additional subsidy resources of SDR 1.5 billion. Staff's updated projections indicate that, notwithstanding this contribution, the Reserve Account could subsidize annual lending of about SDR 0.7 billion on a sustained basis. This is subject to large uncertainties, however, as staff acknowledge that their projections are subject to important assumptions regarding the rate of investment earned on the Reserve Account balance, interest rates paid to lenders, resumption of reimbursement of the GRA for PRGF/ESF administrative expenses, and repayments of overdue Trust Fund, SAF, and PRGF obligations by the protracted arrears cases once their arrears are cleared. [2] Accordingly, we wonder what sources of financing could be considered to replenish the Reserve Account should these assumptions fail to meet staff's expectations? We also question the assumption that the long term self-sustained subsidization capacity of the Reserve Account is based on a reduction in lending capacity from SDR 1.5 billion to SDR 0.7 billion after 2015.

[2] Update on the Financing of the Fund's Concessional Assistance and Debt Relief to Low-Income Member Countries, SM/09/99, April 17, 2009.

New Bilateral Subsidy Contributions

Potential implementation of the aforementioned proposal implies that additional subsidy resources, estimated at about SDR 0.74 billion would be needed to supplement the Reserve Account subsidization capacity and meet LICs' financing needs over the medium term. Our preference would be for such an amount to be provided for through additional bilateral subsidy contributions. The Leaders of the Group of Twenty have emphasized the importance of addressing the fallout from the global crisis on the Fund's poorest members. We would welcome their contribution by means of additional subsidy resources to help ensure that the Fund has adequate concessional financing capacity to support these members. Clearly, the modest fund-raising effort suggested by staff—SDR 0.1–0.3 billion out of the total additional required subsidy of SDR 1.5 billion—imposes an undue burden on the Fund's own resources.

Delaying GRA Reimbursement for PRGF-ESF Trust Administrative Expenses

Staff estimate that this proposal could generate subsidy resources of about SDR 0.1 to 0.2 billion over three years, assuming PRGF-ESF administrative costs are of the order of SDR 50 million per annum. The Board decision on the new income model indeed provides for such delay if the resources in the Trust are likely to be insufficient to support anticipated demand for PRGF-ESF assistance and the Fund is unable to obtain additional subsidy resources. Like Mr. Kiekens, however, we remain to be convinced that efforts have been exhausted to obtain additional subsidy resources. Were this option to be pursued, the period for which reimbursement is suspended should not exceed three years, covering the peak concessional lending period associated with the current crisis. Beyond this period, the Fund's medium-term income position would be negative in 2015 under the baseline scenario, as indicated in paragraph 13. This would render the option inconsistent with the objectives of the income model. An additional safeguard could be that the option be automatically suspended should GRA income decline below a certain threshold. We would be grateful if staff could consider such modalities in their future work.

Profits from Gold Sales

Profits from gold sales would, in our view, undermine the integrity and sustainability of the new income model. The latter provides for the creation of an endowment with the profits from a limited sale of gold. Such profit represents assets of the GRA, as noted by staff, and cannot be transferred to subsidy accounts for the benefit of only low-income members. All three options require the staff to prepare a package of decisions that may need to be resubmitted for approval by the membership. In what follows we elaborate our concerns with the three options presented by staff.

Option 1. Use of windfall gold profits. This option proposes to make available part or all of any windfall profits from higher-than-assumed gold prices as subsidy resources. As noted by staff, however, there is no certainty that the Fund will indeed obtain a windfall profit from gold sales. Most importantly, this option runs counter to the new income model's objective that "all profits from these gold sales should be placed in the Investment Account and invested with the objective of generating investment returns to contribute to the Fund's income while preserving the long-term real value of these resources."

Option 2. Use of net investment income from gold profits. This option consists in retaining the gold sales profits in the Investment Account but using part of the investment income from the endowment to provide subsidy resources. An important risk in this connection consists in using future income to provide subsidies, which could lead to operational losses in the GRA, as highlighted by staff. In the case that there is a consensus view to use profits from gold sales, this option would seem the least detrimental to the objectives of the new income model. Here again, we would suggest that this option be time-bound to the period of exceptionally high income (beyond a pre-determined threshold).

Option 3. Use of a pre-determined amount of gold sales proceeds. This option provides for the transfer of a pre-determined amount of resources from the Investment Account that is linked to gold sales proceeds to finance LIC subsidy needs. In this case, the full risks of a lower gold sales price than assumed in the medium-term income calculations would be borne by the GRA. As with option 1, a potential shortfall in the GRA account would hamper the Fund's capacity to carry out its strategic functions effectively, and would thus be inconsistent with the objectives of the new income model.

It is clear from the discussion above that extensive additional work will be needed to flesh out the full implications of the various options presented in the staff paper. We might also want to consider collectively whether new bilateral subsidy contributions should not play a much larger role than currently envisaged in securing the needed subsidy resources over the medium term. This would be the most transparent and appropriate course of action from the point of view of safeguarding the Fund's mandate and income position.

With regard to additional loan resources that need to be mobilized over the medium term, we see scope for further exploring lending of SDRs to the PRGF-ESF Trust, in the context of a general SDR allocation of US$250 billion.

Mr. Itam submitted the following statement:

We need to emphasize at the outset that the Fund resource envelop being contemplated for the LICs to address their needs arising from the current crisis, which is not of their making, is miniscule relative to the resources that have been mobilized and proffered for the use of the rest of the membership including emerging market economies. The contrast of the SDR 11.5 billion for the LICs for a period of seven years as opposed to the close to a trillion dollars for the rest of the members cannot be sharper. This may suggest not only that the estimate of the resource requirements that need to be availed by the Fund is clearly understated but also reflect the priority or lack thereof, the institution places on its support to LICs.

Our grays on LIC facilities and on Modification of Access Policies for the Poverty Reduction and Growth Facility and Exogenous Shocks Facility expressed our ongoing concerns that:

- the impact of the crisis on LICs may have been underestimated: the contraction of export demand, downward trend in commodity prices, the almost drying up of investment flows can become more protracted than current projections suggest;

- the demand on Fund resources have been computed on the basis of the proposed increase in access limits and norms, which we have argued to be inadequate; and

- the staff should have been in direct contact with our authorities to appraise their likely current and projected needs arising from the crisis.

Accordingly, we are of the view that staff projections on need and demand for resources may be overly conservative.

We consider that staff may have taken an overly pessimistic view about the resources that can be mobilized from bilateral contributions. The recent G20 leaders' summit evinced considerable commitment from them to meet needs of LICs. What is required from the Fund is a rigorous estimate of the needs, which is then used to adjust access limits and norms to compute demand and to mobilize the resources from members. We would argue that the Fund should, besides approaching advanced economy members, target emerging market members who are in relatively strong positions to contribute, given their relatively strong reserves positions. Failure to do so poses significant reputational risks for the Fund.

We would support delaying the reimbursement of the GRA for the administrative expenses incurred by the Fund in providing concessional support to LICs. We need to reiterate a point we had made previously that the Fund should cover the administrative expenses of the PRGF-ESF Trust from its operational expenses.

Concerning proceeds from the gold sales, we prefer option 3, namely that a pre-determined amount of the proceeds be used to finance LIC subsidy needs.

The current approach for mobilizing concessional resources, where these are seen as an “add on” that is managed differently from GRA resources, would periodically lead to them being inadequate and, concomitantly, a need for rationing. This approach may need to be changed, and the present circumstances provide an opportune moment to do so.

Mr. Mojarrad and Mr. Rouai submitted the following statement:

We thank staff for identifying options for possible sources of subsidy financing for the Fund's concessional lending through FY2015. We note that these options are based on the scenario of doubling of the Fund's concessional lending capacity. We may need to consider an alternative scenario involving higher subsidy needs if the Board agrees to a level of access under LICs' facilities higher than the one proposed by staff. It is also reasonable to expect a number of LICs to graduate from concessional financing over the projection period, thus offsetting the aggregate need for subsidy. Overall, we accept the working assumptions of additional loan resources of SDR 9 billion and subsidy needs of SDR 1.5 billion.

We agree with staff that loan resources are easier to mobilize. In this connection, we encourage staff to explore the option of using part of the SDR allocation for lending to the PRGF-ESF Trust.

With regard to subsidy resources, it is clear that the sale of gold is the primary source, as highlighted by staff. This increases the urgency of ratifying the new income model framework and agreeing on, and proceeding with, the sales of gold.

On bilateral contributions, staff seem to downplay the ability, and responsibility, of bilateral donors arguing that "it may be unrealistic to seek the full amount of subsidy resources through bilateral contributions" because of tight budget constraints. This may be true. However, if bilateral contributions are not pursued forcefully, benefiting from the current favorable political momentum following the G-20 Summit, the Fund may end up assuming the totality of the subsidy bill. Therefore, we encourage management and staff, to intensify their fund raising efforts and call on the Board and individual Executive Directors to support these efforts.

One of the options proposed by staff is the transfer of SDR 0.74 billion from the PRGF-ESF Reserve Account (RA) to the PRGF-ESF Subsidy Account. This will cover half of the subsidy needs. Staff concludes that, even with such a transfer, resources in the RA are enough to self-sustain subsidization of about SDR 0.7 billion of annual PRGF commitments after 2015. We can support such an approach and we appreciate if staff could confirm that this implies that the self-sustained PRGF will start in 2015.

Staff is also proposing to delay GRA Reimbursement for the PRGF-ESF Trust Administrative Expenses. In view of the recent improvement in the Fund's income position, and pending successful completion of the PRGF financing drive, which should also cover the cost of reimbursing the GRA, we can support delaying for three years these reimbursements. We hope that such a decision will not weaken the Fund's efforts to mobilize subsidy resources nor potential donors' readiness to contribute. We support the comments made by Mr. Kiekens on the importance of transparent accounting of the cost of administrating the PRGF ESF Trust.

Staff is proposing three options on how to use part of the proceeds from gold sales to subsidize Fund's concessional lending. We understand that these options will involve distribution to all members and re-transfer from all members of the amounts involved. Such distributions could be from the Fund's net income or from the general reserves. We are open to staff operational suggestions in this area. However, these distributions should be presented as part of the proposal to use gold sales to subsidize concessional lending and not as part of a dividend policy. The latter has not yet been considered by the Board.

We favor option 3, involving the transfer of a pre-determined amount of resources from the IA to the GRA for distribution to members. This option offers a number of advantages compared to the two others, including more up-front certainty. Like option 2, however, option 3 could expose the GRA to risks if gold sales prices are lower than assumed in the medium-term income calculation. It is important for the sake of transparency to identify any indirect contribution the GRA may end up making in the process of raising subsidy for concessional lending through gold sales. We encourage staff to further consider this issue and identify ways to isolate the GRA from such risks.

Finally, we appreciate staff analysis on the consistency of the proposed financing options with the new income model. It is important to remember that the new income framework was approved with the objective of setting Fund finances on a sustainable basis. At that time, the Fund was requested to undergo a major restructuring, on which the institution has already delivered. On the other hand, we note that changes are being introduced in the new income model even before its adoption. However, we can accept these changes because we consider that the Fund, as a cooperative international institution, should operate with pragmatism for the benefits of the membership, in particular LICs.

Mr. Alazzaz submitted the following statement:

I thank the staff for a concise and well-written paper that explores possible options for mobilizing the additional subsidy resources needed to support a doubling of the Fund's concessional lending over the medium term. Since the discussion is taking place at a very short notice, I will make some preliminary observations and look forward to a more detailed consideration following the Spring Meetings.

According to the staff, the projected demand for the Fund's concessional financing, after taking into account the proposed increase in access limits and the plans to improve the flexibility of the Fund's concessional lending facilities, could average around SDR 2 billion per year in 2009-2010 and SDR 1.5 billion per year thereafter against an annual average of SDR 0.7 billion in 2000-08. I also note the assessment that the Fund has sufficient subsidy resources to meet projected PRGF-ESF loan demand for the next two years, but efforts are required for meeting the subsidy needs for projected demand for concessional lending through 2015.

Against this background, various financing options have been presented in the paper, including additional bilateral contributions, delaying reimbursement of the GRA for PRGF-ESF administrative costs, and use of part of the income stream or profits from the agreed gold sales. As regards new bilateral contributions, the staff notes that it may not be realistic to seek the full amount of subsidy resources needed, given very tight budget constraints for donor countries in the context of the global economic and financial crisis. Indeed, even the limited subsidy resources-raising effort mentioned in the paper could turn out to be ambitious in the present circumstances.

On the resumption of reimbursement of the GRA for the expenses of operating the PRGF-ESF Trust, the suggestion to delay it for a specified period, which will be consistent with the Board Decision No. 14093-(08/32), is worth pursuing. Here, delaying reimbursement for 3 years appears reasonable, as it will cover the period of peak concessional lending as well as the period when the non-reimbursement could be more easily accommodated.

Turning to options for using part of the proceeds from the agreed gold sales (or the resulting investment income), it is clear that each option has advantages as well as disadvantages. Option 1 is most in line with the new income strategy, but it leaves uncertainty regarding the availability of subsidy resources. While option 2 has the advantage of preserving the corpus of the gold sales profits as capital in the endowment, the sustainable payout ratio from the endowment and thus the amount of subsidy resources is also uncertain. Option 3 would provide upfront resources, but it could negatively impact the new income model if the actual average sale price falls short of $850 per ounce. The uncertainties related to the price of gold or the investment income is further compounded by uncertainties regarding the level of Fund lending over the medium term and the need for precautionary balances. Against this background, while we should upfront declare our commitment to utilize one or more of the above noted options to provide the needed additional subsidy resources and thus remove uncertainty regarding this issue, I would not rule out any of the three options at this stage, especially as there are sufficient subsidy resources to meet the projected PRGF-ESF loan demand for the next two years.

Mr. Kishore and Mr. Choudhary submitted the following statement:

We thank the management and the staff for bringing this analytical paper to evaluate the resource needs and financing option for significant augmenting of the Fund's concessional lending capacity.

Staff projects that the demand for the Fund's concessional financing, which is expected to double over the short and medium term. Demand is projected at SDR 2 billion per year over the next two years and about SDR 1.5 billion a year (double the 2008 level) thereafter until 2015. Staff does not anticipate much difficulty in raising new loan resources of almost SDR 9 billion, as the Trust is able to borrow quite easily.

The main difficulty is expected to arise in meeting the additional subsidy resources of about SDR 0.74 billion ($1.05 billion approx) over a 5 year period – i.e. approximately $200 million per year. Donors are more reluctant to provide grant funds to subsidize the on-lending to low income countries.

Financing Options

Fund should make all out efforts to seek additional subsidy resources from advanced and resource rich countries. However, we concur that it would not suffice and yield much.

As far as delaying GRA reimbursement for PRGF-ESF Trust administrative expenses is concerned, we have reservations. Revival of reimbursement was part of the new income model and we feel that reversing the decision so quickly will not be an appropriate precedent.

On utilizing a portion of the proceeds of the gold sale already approved, we would be inclined to support Option 2 i.e. retain the gold sale profits and use part of the investment income from the endowment to provide subsidy resources. This approach would be more consistent with the new income model than the other two. As part of the New Income Model, there is already a provision that excess income should not be retained by the Fund and should instead be distributed as dividends to members. It is expected that with the higher prices of gold, the income from the investments of the higher proceeds would exceed the Fund's needs and this additional income, instead of being distributed as dividend could be used to subsidize LIC lending. Will this extra income be adequate to meet the additional requirement of subsidy resources? Staff may clarify.

Mr. He and Ms. Lin submitted the following statement:

We thank staff for producing the concise paper within such a short time frame following the call from the G20 Summit—which is intended to address a bottleneck issue in the ongoing reform on the concessional lending framework.

As indicated in the companion paper, the near-term gap in concessional loan resources looms even without an increase in the access policies, and pending greater flexibility in the concessional lending framework, which requires a prompt mobilization of loan resources. Even though loan resources have been traditionally easier to mobilize than subsidy resources, the difficulty and urgency of the fund-raising exercise should not be underestimated given that many members are facing tight budget constraints in the context of the global economic recession. We urge staff to take up this issue as early as possible and encourage developed countries to assume greater responsibility in delivering financial support to the LICs.

We are concerned about the use of the PRGF-ESF Trust Reserve Account to subsidize new concessional lending once the available subsidy resources are depleted. The purpose of establishing the Reserve Account is to provide security to PRGF-ESF Trust lenders in the event of a delay or non-repayment by PRGF-ESF borrowers. As lending demands from LICs are likely to increase significantly as the global environment deteriorates along with enhanced flexibility in the concessional lending framework, the risk associated with a delay or non-payment is on the rise accordingly, necessitating sufficient resources to safeguard the interest of lenders before the initiation of the self-sustained subsidization operation. In addition, the resources necessary to ensure the long-term self-sustained subsidization capacity of the PRGF-ESF Trust Fund might be higher than estimated due to its sensitivity to key parameters.

The basic principle behind the resumption of reimbursement of the GRA for the expenses of operating the PRGF-ESF Trust is that credit intermediation should not be used to finance other Fund activities such as discretionary financial assistance to the LICs, which constitutes a key element of the new income model. However, we can go along with delaying this reimbursement in light of the insufficiency of concessional resources to meet demand from the LICs as a result of the global recession and the limited availability of bilateral subsidy contributions. On the period for this delay, we prefer a shorter one, say, three years, as the Fund's medium-term income position is subject to high uncertainty and would be negative in 2015 if PRGF-ESF reimbursement was suspended for 5 years under the baseline scenario.

We appreciate staff's examination of three possible options for using part of the proceeds from the agreed gold sales to support the Fund's concessional financing. Each of the three options presented here would require decisions to allow for indirect transfers of these resources. At this stage, we are open-minded to all the three options and encourage the staff to do more research to make sure these financing options are truly consistent with the new income model given the temporary nature of income-boosting from lending even in the high lending scenario and heavy reliance of the new income model on the uncertain proceeds of planned gold sales.

Mr. Legg and Mr. Thompson submitted the following statement:

In today's discussion we are asked to balance the integrity and long-term sustainability of the new income model with the Fund's capacity to meet a likely increase in demand for concessional lending from low-income members adversely impacted by the global economic crisis. We welcome the staff paper which identifies various options for supplementing PRGF-ESF resources, and are pleased it has been brought to the Board so soon after the London G-20 Summit, consistent with the urgency we attach to this issue. At this early stage in the process, all options for increasing resources should be on the table and should be thoroughly explored. We then look forward to more concrete proposals being brought to the Board shortly after the Spring Meetings based on today's initial discussion.

While there is likely to be a significant increase in demand for concessional finance in the period ahead, we should also acknowledge that it is difficult to accurately project demand given the huge uncertainties associated with the current crisis. As such, the financing framework we eventually decide on should be sufficiently flexible to accommodate both higher and lower demand in the future. In this context, we would be interested in knowing whether staff's demand projections take account of the impact of the proposed general SDR allocation and the special SDR allocation under the Fourth Amendment, which will increase the SDR holdings of low-income members and, in doing so, possibly lower their demand for financing.

Based on their demand projections, staff estimates that additional loan resources of SDR 9 billion will be needed through 2015. While staff is confident of being able to raise these additional loan resources, we would still encourage them to explore options for members to lend or donate any SDR allocation they may receive to the PRGF-ESF Trust.

Staff estimate that roughly half of the additional SDR 1½ billion of subsidy resources needed to meet projected demand for concessional lending over the medium-term can be met by a transfer from the PRGF-ESF Trust Reserve Account, while still leaving enough funds in this account to ensure its long-term self-sustained subsidization capacity at about SDR 0.7 billion per year.

New Bilateral Contributions

To meet the remainder of the needed subsidy resources, the Fund should, in the first instance, aim to mobilize additional bilateral donor contributions. We recognize that this may be more difficult than usual given the current fiscal pressures being experienced by many countries. As such, we would encourage the Fund to try and widen its list of donors by targeting non-traditional donors, some of whom are in a stronger position to provide funds relative to some traditional donors. To assist the process, we would also urge the Fund to take forward its proposals outlined in SM/09/55 to move fund-raising to a more structured and regular cycle, and to implement a simplified and more flexible financing structure. The goal should be to raise as much as possible in bilateral subsidy contributions so as to reduce the need to tap GRA resources.

Delaying GRA Reimbursement for PRGF-ESF Trust Administrative Expenses

The resumption of GRA reimbursement for the expenses of operating the PRGF-ESF Trust was an integral part of the new income model which we supported. However, our support was on the basis that reimbursement of the GRA would not jeopardize the PRGF-ESF Trust's capacity to meet demand from low-income members, assuming other options for raising subsidy resources had been exhausted. Given the projected demand for concessional lending, and assuming a concerted bilateral fund-raising effort, we are willing to consider a further delay of GRA reimbursement, which would be consistent with the decision that was taken in the context of the new income model. Our preliminary assessment is that a three year suspension strikes the right balance in terms of maintaining a sustainable medium-term income position.

Profits from Gold Sales

The new income model was formulated on the basis that gold sales would take place at an average price of US$850 per ounce. Therefore, to uphold the integrity of the new income model, and consistent with the G-20

Leaders' commitment, only gold sales above $US850 per ounce should be considered "additional" and therefore available to subsidize concessional lending.

Among the options for the use of gold sale profits to supplement subsidy resources, option 3 involves a pre-determined appropriation of profits in advance of the actual sales, thereby putting the risk of a lower gold sale price than envisaged by the new income model onto the GRA. Options 1 and 2, on the other hand, put this risk on the PRGF-ESF Trust. Relative to the first two options, option 3 provides greater upfront certainty about the availability of concessional resources.

If the Board decided to pursue option 3 in the interests of providing greater upfront assurance about the availability of concessional finance, then it raises the question of what we would do in the event that the ultimate transfer to the GRA when the gold is eventually sold falls short of the gold sales revenue projected at the time the new income model was decided. If this were to jeopardize the sustainability of the new income model then we need to consider what the options would be for reimbursing the GRA. We would welcome staff's comments in this regard. We would also be interested in knowing what the average gold sale price would need to be such that after the SDR 0.6 billion distribution from gold proceeds assumed in Table 5, the residual profits would be at least as much as was projected when the new income model was decided.

Other Issues

In order to effect the use of profits from gold sales to subsidize concessional lending, staff will need to fully explore the modalities associated with distributing GRA resources to members in proportion to quotas and having them returned as subsidy contributions. Our main concern with this process is minimizing the potential leakage. Though staff outlines some reasons why we might expect leakage to be relatively low, we would still hope that if this approach was followed that all members, even low-income members, would commit upfront to returning their GRA distribution as subsidy resources. Low-income members could think of this as the payment of an insurance premium for the availability of concessional resources should the need arise.

Given the highly uncertain future demand for concessional lending, if the Board decides to increase concessional resources, perhaps jeopardizing the new income model in the process, then we should also consider mechanisms for returning those resources if demand turns out to be lower than expected. For example, at a specified time in the future, if the use of concessional resources has turned out to be lower than we projected, then we could have a mechanism for returning to the GRA that part of the excess resources that was generated from gold sales profits or from the delayed reimbursement of PRGF-ESF Trust administration expenses. Importantly, this would preserve unused bilateral contributions within the PRGF-ESF Trust to support future concessional lending, consistent with the donors' original intentions.

Mr. Pereira and Mr. De la Barra submitted the following statement:

At the outset, we claim that the options to be considered for financing the Fund's concessional lending to Low-Income Countries (LICs) must be fully consistent with the G20 Leaders' commitment to provide $6 billion of additional concessional and flexible finance to the poorest countries over 2009-2011.

On loan resources, there is a need to mobilize promptly nearly SDR 9 billion to cover projected demand over the short and medium term. Additionally, subsidy resources of about SDR 1.5 billion will be needed to subsidize projected demand for concessional lending through 2015. However, we underscore that more subsidy resources will need to be broadly deployed for these countries, disproportionately affected by this external crisis. While we are aware this is not an easy task, we are of the view that the Fund has to step up its efforts and use its improved capacity for fund raising to enhance subsidizing facilities for LICs. In this regard, the decision on a general allocation could include a statement inviting countries to voluntarily re-allocate part or all of their SDR to primarily finance subsidy resources or, alternatively, loan resources to the PRGF-ESF Trust. We would appreciate the staff's comments on the options available in this area.

Turning to the proposed financing options, we believe that new bilateral contributions and the use of the Fund's own resources must be part of a package of measures. Bilateral subsidy contributions must continue to play a critical role, while subsidy contributions from gold sale proceeds could be needed after assumed new bilateral contributions linked to a "realistic" scenario and a suspension of the PRGF-ESF reimbursement. We would like to receive some clarification from the staff regarding the numbers put forward on possible bilateral contributions (SDR 0.1 – 0.3 billion) similar to those committed by 11 countries when the ESF was established (2005). We wonder if the staff could explain this baseline scenario more clearly. We consider that delaying GRA reimbursements for PRGF-ESF Trust administrative expenses and partially using the PRGF-ESF Trust Reserve Account (RA) may be part of the new financing scheme, but evidently the Fund cannot solely rely on these instruments. Suspending reimbursement for three years to cover the peak concessional lending period associated with the current crisis is warranted.

Regarding the use of profit from gold sales, clearly Option 1 is not feasible because of the uncertainty of the gold price at the time of selling, given the presence of high volatility associated to this price, which will still prevail in the following months. In the same vein, Option 2 entails time and an amount of uncertainty of the future income from the gold profit investment. Out of the three options, Option 3 seems to be the most appropriate so far. This approach, on which the Board could make a decision to transfer a specific amount from the IA to the GRA to distribution to members with the expectation that these resources would be returned by them as subsidy contributions, would provide more up-front certainty over the contributions to subsidy resources. However, the envisaged portion of gold sales proceeds allocated to LIC subsidy financing seems to be small and not consistent with the G20 Leaders' commitment. We are of the view that the staff's figures mask concerns about the impact of these measures on the new income model. We underscore that the sharp pickup in Fund lending from the GRA under the new lending framework will also produce additional resources. Once again, our main goal must be to ensure that the Fund makes its contributions to provide ample and flexible financing to LICs to avoid long-lasting setbacks to poverty reduction efforts. The bottom line of the Fund's approach to deal with this issue is to follow the commitment of the G20 leaders. We stand ready to further discuss this and other financing options in the immediate future.

Mr. Guzmán, Mr. Umaña and Mr. Cova submitted the following statement:

In our previous statement on modification of access policies for the PRGF-ESF we expressed our strong support for increasing access levels and we therefore agree with the importance of mobilizing additional subsidy resources to support the doubling of the Fund's concessional lending over the medium-term.

We would like to thank staff for its very pertinent paper that incorporates three options that deserve careful consideration. The staff has come up with some proposals regarding the Fund's concessional lending to low-income member countries, resource needs and options, including: 1) new bilateral contributions; 2) delaying General Resources Account (GRA) Reimbursement for PRGF-ESF Trust Administrative Expenses; and, 3) the profits from gold sales. It is a way to respond to the commitments made in the context of the G-20 Summit in London. It can also be seen as part of the efforts to revamp the adequacy of the institutional lending toolkit.

The global financial crisis has had an adverse impact on many economies, including LICs, threatening the hard-earned gains from recent years through the combination of adequate macro policies and structural reforms. This situation highlights the need for exploring options to provide the estimated US$6 billion additional concessional and flexible finance for the LICs over the next 2 to 3 years, as consistent as possible with the new income model, which we considered an important pillar of the overall governance and financial reforms of the IMF. We believe that all three options have merits and drawbacks and that none by itself is sufficient to bridge the gap.

We reiterate our support to the agreed sales of IMF gold, which should take place as of FY2010 and the investment of the proceeds in an endowment account, in order to fulfill the double objective of both generating returns to the Fund's income and preserving the real value of the resources to be obtained from the sales of gold. We are aware of the fact that, as a source of income for the purpose at hand, this modality requires solid commitments from the membership to guarantee that the GRA resources distributed to all members are thereafter returned under the form of subsidy contributions for concessional lending. But this is also essentially similar for any other objective.

On the other hand, under present circumstances new bilateral contributions are uncertain. Moreover, a temporary suspension of reimbursement of the GRA for PRGF-ESF expenses would provide a certain but also insufficient amount. Gold sales could provide a larger amount but we would like to caution against excessive optimism in extremely uncertain and volatile times for commodity prices. We would not want to be left with unfunded mandates. That is why we understand as the most reasonable way forward a combination of the three alternatives that should be designed to provide us with the amount required on a predictable and quasi certain basis.

In this regard:

- The temporary suspension of reimbursement of the GRA for PRGF-ESF expenses should be approved with immediate effect. This was never a central element to the new income model. It was a rather ugly and easy complement to the more substantial changes, which ended up not materializing (investment of a portion of the quota, investment of the proceeds of gold sales). However, we do think this measure should be temporary and a specific sunset clause should be included for this purpose, perhaps connecting the cancellation of the measure with the reestablishment of sufficiency in the PRGF Subsidy Account.

- Among the options presented to use gold sales originated resources, we would favor devoting a conservative portion of the windfall profits from gold sales to LIC financing. We would consider this as a pre-determined amount.

- The sum of the preceding elements would leave a residual which should ultimately be covered by bilateral donor contributions. The IMF should convene members/donors to a pledging session where they would be expected to fulfill the commitments pre–announced at the G20 and other fora.

Mr. Moser and Mr. Weber submitted the following statement:

We note that the financing needs assessment serves primarily as a justification of the G20 agreement that the Fund provide a specific amount of additional concessional financing to LICs. Given that the financing needs will also depend on the envisaged broader reform of the Fund's LIC facilities, it is difficult to make precise projections at this stage.

The uncertainties surrounding the implementation of the new income model and the income ultimately generated from it are worrying (Paragraph 28). We consider it highly problematic to already commit to distribute some of the proceeds to be generated under this model, before concrete progress has been made in either ratifying or implementing it and the Board has not even adopted the decision authorizing the sale of gold.

The proposals for using the proceeds from gold for financing concessional lending runs counter to the key objective of the new income model, which is to put the GRA on a sustainable footing (which includes the building up sufficient precautionary balances) and not to subsidize a trust fund designated to a subset of the membership.

Moreover, during the discussion on the income model, the staff recommended consistency with the five long-standing principles for Fund policies on gold, among them that: (i)As the only asset with a significant unrealized value, gold provides fundamental strength to the Fund's balance sheet; and any mobilization of gold should avoid weakening the Fund's overall financial position; and (v) profits from any gold sales should be retained, and only the investment income should be used for purposes that may be agreed upon by Fund members and are permitted by the Articles of Agreement. It seems to us that these principles limit the options proposed by the staff. The staff's comments would be welcome.

We therefore consider the recourse to new bilateral contributions to be a much more transparent and straightforward method to mobilize additional subsidy resources – if needed –, with no indirect effects on other financial mechanisms. Such bilateral fundraising can be well justified in substantiated exceptional circumstances. It would mitigate risks from volatile gold prices and safeguard the Fund's new income model.

If the use of the proceeds from gold sales remains the preferred way forward for the majority of the membership, we would insist on as much transparency and as few distortions of the Fund's financing principles as possible. We also believe that the proposed suspension of the reimbursement of the GRA for PRGF-ESF expenses would perpetuate an undesirable distortion in the system and be less transparent. The decision to resume the reimbursement has been an integral part of the new income model and should not be reversed.

Our main preoccupation regarding the financing of concessional lending has consistently been to build a self-sustaining model. We regret that this objective is being postponed once again.

Mr. Sadun and Ms. Valeri submitted the following statement:

We thank staff for their comprehensive paper and for the proposals on possible options for mobilizing the resources needed to finance a doubling of the Fund's concessional lending capacity. The options presented in the paper provide an appropriate follow-up to the Board discussion on the financing framework for LICs.

At their recent meeting in London, the leaders of the G20 called on the IMF to come forward with concrete proposals to provide $6 billion of additional concessional financing for the poorest countries over the next three years in a way consistent with the Fund's new income model. The staff paper responds to this request and explores possible sources of financing, including delaying reimbursement of the GRA for PRGF-ESF administrative costs, proceeds from gold sales, and additional bilateral contributions. We believe that any proposals should be consistent with the objectives of the new income model and the G20 commitment. Accordingly, we offer the following comments.

Delaying GRA Reimbursement for PRGF-ESF Trust Administrative Expenses

We agree that conditions are in place for a temporary suspension of the GRA reimbursement for PRGF-ESF administrative costs. This reimbursement should be suspended only for three years, covering the peak of concessional lending demand associated with the current global crisis. Staff states that, based on the current estimates, the delay of the GRA reimbursement for PRGF-ESF administrative costs can generate subsidy resources of SDR 100-200 million over 3 years. In this respect, we agree with Mr. Kiekens that a transparent cost-accounting framework that assesses with clarity the costs of the different tasks of the Fund staff, including costs related to PRGF-ESF operations, should be useful in order to make a correct estimate. We invite staff to update the Board on progress in this regard, in time for the next Board discussion on the Fund's income position.

Use of Profits from Gold Sales

The new income model requires all of the proceeds from gold sales to be allocated to an endowment and invested in order to generate income. Under all three options presented by staff, resources from gold sales or the proceeds from the resulting profit's investments will be used to support the Fund's concessional lending. Under option 1 there exists a risk of not obtaining the envisaged funds, while options 2 and 3 better guarantee the expected resources. Therefore, the latter two options seem to be preferable in mobilizing the required financing. However, under option 2, resources would be generated only after some time following the sale of gold and the investment of the gold proceeds, and this will negate the urgency of the assistance as requested by the G20.

New Bilateral Contributions

We believe that the target of SDR 100-300 million in additional bilateral contributions mentioned by staff is somewhat optimistic given the high budget constraints that many donors are facing in the context of the recession. However, good burden-sharing can contribute to a successful fundraising. In this regard, a proposal should be elaborated on encouraging member countries to contribute through bilateral contributions in a fair burden-sharing basis for the needed subsidy resources.

Mr. Chua and Mr. Thapa submitted the following statement:

Staff pointed out that projected demand for concessional lending would reach SDR 11.5 billion through 2015. They estimate that SDR 9 billion will need to be mobilized for loan account and SDR 1.5 billion for subsidy account. As we mentioned in our statement on the increase in access limits for the ESF and PRGF, we believe that the additional demands on the Fund's resources should be fully financed on a sustainable basis. We are open to exploring all the options mentioned in the paper to mobilize the needed resources for concessional financing and would not rule out any of them at this point.

Bilateral Contributions

Like Mr. Legg and Mr. Thompson, we believe that the Fund should, in the first instance, aim to mobilize additional bilateral donor contributions. We suggest that the management make an urgent call to all possible donors, particularly G-20 members, to contribute or expand their contributions to the needed resources for concessional financing.

We note, however, staff's view that mobilizing all needed resources via bilateral contributions will be difficult given the current economic circumstances. In this regard, has staff identified the potential lenders for mobilizing the required resources for low income member countries? We also join Mr. Pereira and Mr. De la Barra in seeking staff's comments on options in relation to inviting countries to voluntarily re-allocate part or all of their proposed SDR general allocation to finance subsidy resources or loan resources to the PRGF-ESF Trust.

Suspension of GRA Reimbursement for PRGF-ESF Trust Administrative Expenses

In light of the exceptional circumstances that we face today, we are also open to considering a further delay of GRA reimbursement for PRGF-ESF Trust administrative expenses. Furthermore, in a broader perspective, we would ask the management to consider the feasibility and desirability of a policy of setting aside a certain percentage of income generated from the GRA for the subsidy resource account on a regular basis. This option may provide a more reliable and sustainable source of income for subsidy resource account.

Profits from Gold Sales

We are open to the options proposed by staff in this regard. We also urge management to be responsive to members' needs regardless their sizes and their level of development, and thus pragmatic in allocating income, inter alia, generating from the gold sales proceeds. Among three options proposed by staff, Option 3 – i.e. transferring a pre-determined amount of resources from the IA linked to gold sales proceeds to finance low income member countries' subsidy needs – appears the most promising in addressing short-term and pressing financing needs effectively and in a timely manner. That said, we note that this would create a risk of a lower gold sale price than envisaged by the new income model. At the same time, the uncertainties surrounding options 1 and 2 raise questions about their timeliness and effectiveness in responding to the aforementioned issues. We would therefore suggest that staff continue to further develop the appropriate modalities for securing subsidy resources on a sustainable basis.

Mr. Horgan and Mr. Ladd submitted the following statement:

We thank the staff for a tightly-focused paper on options for mobilizing the resources needed to fulfill the G20 Leaders' call to double the Fund's concessional lending capacity.

Loan Resources

The staff points out (Para. 5) that the new general SDR allocation that G20 Leaders called for could provide a source of funds for additional loan (principal) resources. Given the purposes for which the new general allocation is intended (to increase global liquidity), the nature of the SDR (a reserve asset), and that a significant proportion of the new allocation will be provided to developing economies in general and low-income members in particular, we would be averse to considering our incremental SDR allocations as a source of funds for concessional loan resources.

PRGF-ESF Trust Reserve Account (RA) and New Bilateral Contributions

We would be comfortable with the proposed allocation of SDR 0.74 billion from the RA to cover half the estimated additional subsidy needs to 2015 (Para. 8). Postponing the achievement of self-sustainability of the PRGF-ESF Trust for a few additional years is reasonable under the circumstances.

In terms of new bilateral contributions (Paras. 10 and 11), any additional concessional resources still needed after investment income from gold sales and higher than expected lending income (after provision for risk) should be raised through a regular replenishment process that features equitable burden-sharing among the membership.

Profits from Gold Sales

The G20 Leaders' communiqué noted that any contemplated use of additional gold sales should be consistent with the new income model. This is critical. Of the three options presented, it would appear that Option 2 (retain all the gold sales profits in the Investment Account, but use part of the investment income to provide subsidy resources) is the most compatible with the IMF's traditional gold policy (preservation of the corpus of profits on gold sales) and provides the most security to the Fund's medium-term financial sustainability. This is most consistent with aims of the new income model.

Option 2 also appears to minimize the opportunity for "leakage." There would be a regular stream of investment income to be transferred back to members, to be returned as subsidy contributions, all under the watchful eyes of the Executive Board, on a repeated-game basis. Options 1 and 3 appear riskier (windfall profits may not materialize, risks of a lower gold sale price being borne by the GRA, greater leakage). We recognize that Option 2 may be the relatively slow approach to ramping up concessional resources, and therefore postponing reimbursement of the GRA for PRGF-ESF expenses until investment income from the gold sales is flowing into the subsidy accounts would be reasonable.

The staff rightly points out (Para. 28) that the new income model is not yet in place and that projected income from lending is highly uncertain. Given the risk associated with the "jumbo" arrangements that the Fund is financing under new and existing instruments, the precautionary balances obviously have first call on higher than expected lending income. If, as the years go by, exposures are reduced, consideration can be given to the redeployment of those resources.

Mr. Kotegawa and Mr. Kihara submitted the following statement:

We thank the staff for presenting a thorough overview of the financing options for the Fund's concessional lending to low income countries.

The statement issued by the G20 Leaders called for the Fund to provide a substantial amount of additional concessional financing. We appreciate the work done by staff to prepare several options in response to this call. Since external environment could change substantially for the near future, we ask the staff to keep various options on the table for the time being, and be flexible to adopt to those changes.

Having said that, we think the presented option follows the opposite of what would be the logical flow by: (i) expecting additional bilateral contributions, (ii) adding more resources from the suspension of GRA reimbursements for the administrative expenses of the PRGF-ESF Trust, and (iii) filling the unfunded gap by profits stemming from gold sales. As the Staff Paper acknowledges, the current severe economic downturn has placed member countries' fiscal balance in an extremely difficult situation. Future consideration on financing options will need to be mindful that many countries could face difficulties with tax payers to allocate additional resources to areas outside of economic stimulus.

Instead, we encourage the staff to maximize the benefits derived from the additional revenue from increased GRA lending and the higher gold prices, and to reconstruct the proposal accordingly. Needless to say, due consideration to these factors should be consistent with the new income model.

It is reasonable to temporary suspend the reimbursement due to expected increase in GRA revenues. Nonetheless, the period allowed for the temporary suspension could be longer than that indicated by the staff, if the Fund's financial environment further improves. The Fund might also be able to allocate a larger amount of resources from the profits of its gold sales, although we recognize that, at this stage, there still remains relatively high uncertainty regarding the actual proceeds from gold sales. We ask the staff to explore these possibilities. Fundraising from bilateral donors should be initiated only after having thoroughly explored those possibilities. And such fundraising exercise should aim at substantial increase in the number of contributors, including non-traditional donor countries.

Mr. Bergo and Ms. Mogensen submitted the following statement:

We see the medium-term need for increased subsidy resources for financing lending to low income countries (LICs). At the same time, it is of greatest importance that the agreed new income model is not undermined. We are, therefore, reluctant to use proceeds from the gold sale or to use surplus income for this. Allow us to elaborate:

In the new income model it was agreed that financing for LICs should be primarily financed externally, i.e. through contributions from other members. We believe that this is a much more transparent and straight forward method of financing that should be preferred to the indirect financing through gold and surplus income.

Our constituency has in the past contributed generously to finance LIC lending and is prepared to continue to do so. We call on others to do the same.

We find it too early to make decisions on using proceeds from the gold sale and surplus income, since the new income model is not yet fully implemented. This is also considering that staff at this stage identifies the need to arise in the medium term, not in the short term. However, we are open to return to the topic at a later stage, where we can better judge the opportunities for the proposed additional financing. At that stage, we should also have more clarity on the actual need, including potential additional demand arising from a reform of the toolkit.

On some of the specifics:

- Our preference is to rely on external financing as surplus income from lending should preferably not be used to finance other activities of the Fund. Nevertheless, the use of excess real return from the invested proceeds of the gold sale can be discussed once the endowment is generating an income. Most likely any use of such income must be through dividends, and we would be open to use such dividends to finance concessional lending. However, we are far from there yet, and the key is to move forward with the gold sale.

- The PRGF reimbursement to the GRA may be temporarily waived in the short run, if the circumstances so warrant, as described by staff. We are not convinced that this is the case yet.

In light of the more urgent need for additional loan resources, we find it surprising that this issue is not further discussed in the staff paper. We would welcome staff’s elaboration on how they intend to move forward with this.

Mr. Bakker submitted the following statement:

I thank staff for producing a paper which examines possible sources to support the Fund's concessional lending to its LIC members. To ensure that the Fund responds effectively to the urgent needs of low-income countries in the current environment, it is imperative to strengthen the existing resources of its two PRGF Trusts, as soon as possible. With this goal in mind, I offer the following propositions for the management and staff to explore:

It is critical to approach the potential bilateral contributors immediately, in order to assure that the depleted loan resources are replenished as soon as possible. The proposed ad hoc increase in SDRs may come too late to address the immediate needs for loan resources. Thus, staff should immediately start exploring other options that may be available with respect to indirect lending of a portion of the Fund's general resources to the PRGF-ESF Trust. At the same time, the Management could explore whether the recent bilateral lenders to the GRA may be willing to reallocate a small portion of those resources towards concessional lending.

In the medium term, subsidy contributions would need to be raised as well. In this regard, I support the staff's proposals on using the PRGF-ESF Reserve Account and suspending for 3 years the reimbursement of the GRA account for the PRGF-ESF expenses, if necessary. However, in the interest of fairness and exploiting the momentum from the London G-20 summit, it would be preferable to first call on those countries which currently do not contribute to the Trust but may be able to do so, to provide support.

Regarding the three options put forward by staff for using the profits from gold sales to augment subsidy resources, I note that the first and second options do not diverge too much from the new income model, but these options provide very modest financing, only in outer years, and subject to large uncertainties related to gold prices and investment returns. While the third option achieves a predictable and significant impact, this option could potentially weigh more on the Fund's overall financial position, especially if the bilateral contributions fall short of expectations, leakage is higher than anticipated, and the high GRA lending environment lasts shorter than currently envisaged.

Going forward, I encourage staff to consider how the existing limited fungibility of Fund resources could be addressed more generally. For instance, if a new stand-by-like instrument is created for low-income countries, it is conceivable that, under the existing framework, the Fund finds itself in a situation where it has no resources for such a purpose, while at the same time it has excess resources for some other purposes. It might be worthwhile exploring how donor financing could be made more fungible in the future.

Ms. Lundsager and Mr. Kaplan submitted the following statement:

At their April 2009 Summit, G-20 Leaders committed, "consistent with the new income model, that additional resources from agreed sales of IMF gold will be used, together with surplus income, to provide $6 billion additional concessional and flexible finance for the poorest countries over the next 2 to 3 years." The intent of the G-20 Leaders is clear – special efforts are necessary to ensure that the Fund responds to the current crisis by adequately assisting its low-income members.

The staff's proposal is not targeted at assisting the Fund's low-income members during the crisis. Instead, the staff seeks to fill a possible gap in subsidies for lending that may arise beyond the medium term – from 2011 to 2015 – should future demand for IMF lending be significantly above the experience of the past several years. We believe that the IMF should instead assist low-income countries now and request that the staff explore options that could achieve this.

As we indicated in our written statement (GRAY/09/1397) for yesterday's discussion on increased access levels, there is a case for temporarily increasing the concessionality of Fund assistance to low-income countries, in the context of a surge in crisis-related lending, similar in spirit to how IDA provides assistance to its members at high risk of debt distress.

The Fund must not repeat the mistake of sinking its low-income members in a cycle of over-indebtedness, that we had to correct with HIPC/MDRI debt reduction. Crisis-related needs may be considerable, with demand for financing emerging from the deep shock to exports, growth, and revenues in low-income countries. Debt ratios will be worsening in many countries, some of which are already quite fragile. We believe that the Board needs to consider options to help those low-income countries that require assistance while dealing more directly with the debt sustainability implications of IMF lending through the crisis.

In short, we urge the Board to consider options for using resources from the gold sale and surplus income to increase the grant element associated with LIC crisis-related lending. Directors recall that the Fund's low-income lending is provided at a level of concessionality below, sometimes far below, what the Fund advises its low-income members to seek from other creditors. The currently low interest rate levels have narrowed the degree of concessionality in IMF assistance even further.

Grant resources financed from gold sales and surplus income could be used to greatly increase concessionality consistent with a borrower's capacity to carry debt. Alternatively, grant resources could be used to provide a level of concessionality equivalent to what the Fund would urge from other creditors for all PRGF borrowers. We ask staff to return to the Board with the exploration of these options.

We join Messrs. Gibbs and Thornton in agreeing with the staff's Option 3, namely to designate an amount of resources to transfer to the poorest, insulated from the vagaries of the gold price. In view of the pressing need to respond to the crisis, we urge the staff to begin plans for the distribution from reserves in advance of the completion of the phased gold sale envisaged by the new income model.

Mr. Nogueira Batista and Mrs. Joseph submitted the following statement:

It is critical to obtain the necessary resources to fund and support the financing needs of low-income countries (LICs), particularly in light of the increases in access limits, the broader reforms to the LIC facilities architecture and the impact of the current global crisis on these countries.

The proposal to use a portion of the resources from the PRGF-ESF Trust Reserve Account (RA) to subsidize new concessional lending appears reasonable. Staff indicates that if SDR 0.74 billion is allocated to meet LIC subsidy needs, there would still be adequate resources in the RA to ensure its long-term subsidization capacity. We also agree that the general SDR allocation of US$ 250 billion could provide an additional source of funding. Given the distribution of quotas, about 60 percent of this general allocation would go to developed countries.

Staff argues that in the current difficult economic circumstances, many countries may be hard-pressed to make bilateral contributions to boost subsidy resources. However, this has not impeded the G20 to come forward with ambitious targets in terms of increasing the Fund's general lending capacity. A number of countries have come forward and pledged contributions to the Fund. It would not be understandable if a fund-raising effort could not be made for LICs. Present bilateral contributors to the PRGF-ESF Trust Fund as well as new lenders can be solicited for support. We would prefer to use the amount (SDR 0.1-0.3 billion) suggested by staff as a floor rather than as a target, in order not to put a ceiling on members' pledges and contributions.

We also agree that the reimbursement of PRGF-ESF Trust administrative expenses to the General Resources Account (GRA) should be suspended for the period (three years) suggested by staff, after which the issue can be revisited.

With regard to use of gold sales, our main concern is not to undermine the new income model of the Fund. If that basic concern is respected, we are ready to explore the three options outlined by staff.

Mr. Stein made the following statement:

The Mandate

G20 leaders have recognized that "the current crisis has a disproportionate impact on the vulnerable in the poorest countries" and have assumed "collective responsibility to mitigate the social impact of the crisis" and "to minimize long-lasting damage to global potential".

The commitment of leaders "that additional resources from agreed sales of IMF gold will be used together with surplus income to provide … concessional lending … for the poorest countries" is listed in the communiqué under the heading "Ensuring a fair and sustainable recovery for all".

Clearly, the overall mandate alludes to the shorter, at most medium-term perspective to assist LICs to overcome the crisis by providing access to concessional financing. The time span mentioned in the communiqué says to provide financing over the next "2-3 years". It is, in our view, not intended to have a structured increase of IMF resources to LICs on a permanent basis. Only this short-term focus justifies that IMF general resources are earmarked for only a subset of members, an issue Mr. El-Khouri and Mr. Moser and other directors have rightly pointed to.

Meeting the financing needs of LIC should therefore focus on the immediate time span up to 2011. The staff proposal, instead, seeks to close an assumed financing gap that appears after 2011.

Financing of Concessional Lending

Financing of concessional lending should be “consistent with the new income model”. The three options presented so far all carry risks that compromise full implementation of the new income model. Several directors have pointed to inconsistencies in their grays. Part of the New Income Model is also the GRA reimbursement for PRGF-ESF administrative expenses. However, that is qualified by the condition that the PRGF subsidy account has enough resources to finance concessional lending. If that is not the case, the Board can suspend the reimbursement. With the increased need for concessional lending in the next 2-3 years, the case could be made, that the resources are not sufficient. We are open to look into that matter.

In the long-run, however, it is imperative to build up the Fund’s precautionary balances and even to increase them, given the rising lending and credit demand in this currently uncertain environment.

The options presented by staff explore possible ways of financing additional subsidy needs by gold sales. But, all (three) options carry disadvantages, in particular the risk of being inconsistent with the agreed new income model.

In addition under option 1 and option 2, resources can only be mobilized in the medium-term, as it is still largely uncertain whether there would indeed be “windfalls” from gold sales or sufficient net investment income from gold profits. The question under both options remains, how to “bridge” the financing gap until expected positive “additional” proceeds from gold sales become available. Option 3 for us is not fully in line with G20 agreements. It is an upfront financing commitment which is only indirectly linked to gold sales. Option 3 might be used as a bridge-financing for the additional subsidy resources. Further, we see the disadvantage that proceeds from gold sales have to first be distributed to member states via the GRA investment account. When countries then pledge the resources to the subsidy account the resource transfer for some countries is made through national budgets. Here parliaments have a key role which should not be underestimated and prejudged. Furthermore, on this way back and forth, there is the risk that not 100 % of the distributed resources will be returned.

Therefore I am not in the position to express any preference for one of the options and rather would like to see further elaboration of staff including of other proposals which were made today.

Extending her remarks, Ms. Lundsager said that, following up on the G-20 statement, it was important to provide help to the low–income countries in the immediate timeframe. However, the proposals in the staff report addressed only the medium term, 2011 to 2015. Additional options should be opened up as a way to bring forward some of the benefits so that low-income countries could access resources during the crisis period, given that access limits had just been raised. Increasing the concessionality of PRFG lending by blending grant resources with those in the PRGF Trust would help with the debt sustainability point that many Directors had emphasized in the previous day's Board discussion on modifying PRGF access limits. The staff should take a look at this option.

Mr. Rouai expressed concern that options 2 and 3, if implemented, could shift the problem to the GRA, if the difference between the assumed gold sales and the actual sale price was different. He requested the staff's comments on whether there was any way to cover the GRA, and, if not, the Fund should be transparent that part of the financing was coming from the GRA. He also requested comments on Ms. Lundsager's proposal to pre-finance the gold sales contribution, before the conclusion of the gold sale.

Mr. Fayolle made the following statement:

> First, I would like to thank staff and management for going ahead very quickly on this important issue. I think it is timely and it is necessary to show the poorest part of the membership that we do care about what is going on in their countries.
>
> Back to the technicalities, my preliminary views and those of my authorities, are that, first, we would support use of the Reserve Account as suggested in staff's paper.
>
> Two, we certainly would welcome giving up the reimbursement of the GRA for PRGF–related administrative costs. We did not like it in the first instance, so we would very much welcome coming back to what should be the norm and we would welcome for a suspension for the next five years.
>
> Three, we think it is important to get bilateral resources, and we think it is important that this is done in a way that would make it possible for those countries that have not contributed to the extent they should have to contribute now.
>
> Fourth, in terms of options, this is preliminary, but I think, the way the report is structured, it indicates that the option 3 is the best option, and there is value in that.

One of my problems is that it is very complicated to understand what the average gold price in this paper is. Where does footnote 13, which assumes a price of $810, come from?

Finally, I would join Ms. Lundsager in saying that it would be good to use this opportunity to increase the level of concessionality of the PRGF, which we have discussed in previous discussions.

Mr. Ladd remarked that his chair was comfortable with the use of resources from the Reserve Account and the intention to raise new bilateral contributions. He favored option 2, as the option which gave the greatest primacy to the income model, but was not opposed to option 3, if that was what the Board wanted to move ahead with. Proposals to increase the concessionality of the Fund's lending to low-income countries would be welcomed.

Mr. Bergo made the following statement:

Thank you for an interesting but preliminary paper.

The staff has my sympathy in trying to interpret the G-20 leaders' views as expressed in their communiqué and reconcile that with the new income model. Like Mr. Stein, I am not sure that they have succeeded in every respect on that score.

We are, like Mr. Moser and some other Directors, deeply worried that the new income model will be undermined before it comes into operation. We feel free to disagree with the G–20 communiqué, as we have no ownership of that.

Actually, we think this is to some extent putting the cart before the horse. Under the proposals, we would start spending income that we have not got and we would start also reserving capital for certain purposes, capital that has not been realized.

We remain faithful to what was agreed when we agreed on the new income model, that financing for low–income countries should primarily take place externally through bilateral contributions. That in our opinion remains the best solution, certainly. It is the most transparent and does not compromise the income model. And, it could become available quickly.

When we are skeptical about the ideas posed here, it is not out of a lack of concern for the low–income countries. Our credentials are quite good there. If I am not mistaken, this constituency is the second largest donor in the world. But, we also have to recognize the risk that sufficient bilateral contributions will not be coming forward. In due time, once the income model has been implemented, we would be willing to consider, for instance, using dividends to finance contributions to concessional lending. However, in our opinion, we should really have the income before we start using it.

I apologize for having issued our gray so late this morning. These remarks were actually additional to what we have in our gray.

Mr. Rutayisire made the following statement:

First, let me begin by appreciating the kind of realism that the staff have maintained when writing this paper. At some point, they have mentioned that crises affecting low-income countries tend to stay on longer than could be expected in advanced countries: What I am hearing from those who say that Fund intervention should be short term tends to ignore this realistic assumption. I felt that when the staff went beyond 2011, they anticipated that these countries could not overcome the crisis at the same rate as we could have expected in the case of other countries. I would plead that this perspective be maintained.

Secondly, on the issue of fund raising, I see that this is overly pessimistic. We should be optimistic. I think we cannot prejudge that bilateral donors would not contribute. I think we should be as aggressive as possible.

On the issue of gold sales and allocation of some of the proceeds to the concessional window, I had the same problem as Mr. Stein, but I also remember that in the case of Liberia, these were SCA resources. These were resources after burden sharing. But, in this case, I am told that the gold that is going to be sold belongs to the Fund. So, if the Fund wants to distribute dividends to members, I thought that distribution of dividends should come after all deductions have taken place. I would appreciate an explanation as to why we need to go to the membership in this case, if we do not go to the membership when we want to pay the expenses of running the Fund.

Mr. El-Khouri stated that he agreed with everything Mr. Bergo had said. He noted that it had been very difficult to get agreement on the income model, and that changes were starting to be made even before the new model had been realized. As a matter of principle, the reimbursement to the GRA and gold sales were not elements that should be tinkered with. He accepted the transfer of funds from the Reserve Account, but required assurances about the self-sustaining nature of the PRGF-ESF Trust after 2015. If donors wanted the Fund to lend at a concessional rate, the donors should provide the resources, rather than telling the Fund what to do with its own resources.

The Chairman (Mr. Strauss-Kahn) said that it was clear that the income model should not be undermined. Perhaps some options which did not appear in the paper could be looked at in the coming days or weeks. He had fought hard at the G–20 meeting to obtain a reference to the new income model in the communiqué. He also encouraged Directors to comment on the proposal to increase the concessionality of Fund lending to low–income countries.

Mr. Stein indicated that he supported all of those who said that bilateral contributions should be the main contributor to the Subsidy Account. It was only the focus of the short term which permitted a deviation from that, but in the long run the Fund would need to come back to bilateral financing.

The Director of the Finance Department (Mr. Tweedie), in response to comments and questions from Executive Directors, made the following statement:

> There was a question on the demand projections, whether they explicitly take account of the possibility of a general SDR allocation. This issue was addressed yesterday in the discussion of access limits. We are using the same projections in that paper, as was mentioned by the staff yesterday. No explicit provision was made for an SDR allocation in the projections, but the thinking is that an SDR allocation would help countries to build a reserve cushion and would not be a substitute for concessional lending from the Fund. That is also reflected in the summing up on the modification of access policies for the PRGF and the ESF that was read out this morning.
>
> On the loan resources, there were some questions about how far we have gone in identifying potential lenders. We have not really started this. It is now becoming a matter of urgency, as we point out in the paper, so we plan to start that very soon.
>
> It is some time since we have done this. We have not had a general fund–raising for loan resources in almost ten years. Thus, we do not have recent experience with this. As we have noted in the paper, traditionally it has been easier to raise loan resources than subsidy resources, but, as Mr. Kotegawa cautioned us yesterday, that this does not mean it will be straightforward.
>
> On the question of whether the possible SDR allocation could play a role in that regard—this was raised in the paper and some Directors picked up

on it. It is an issue that we will need to look at. Mr. Hagan may want to follow up on that.

In terms of the general options for using an SDR allocation, if it were to provide loan resources to the PRGF-ESF Trust, what we would envisage is that it would be done in a way that it did not have any cost to the member providing the SDRs. The PRGF-ESF Trust would pay the SDR interest rate. Of course, if it were subsidy resources, which would mean either donating the SDRs or providing them at a lower interest rate, then there would be a net cost for the member providing them.

On the options for generating subsidy resources, the main focus in the paper is on using part of the proceeds from the agreed gold sales. This was a specific request coming from the G–20 summit, so that is where we focused the paper.

As the Managing Director said, we have tried to look at the options in terms of what could be done consistent with the new income model. That was always a starting point.

There were differing views on the extent to which we could expect to rely on subsidy contributions from bilateral contributors. The early sense we have is that there is interest from some members in providing subsidy resources, but it is too early to have a sense of what is feasible to expect from this source. The numbers we put in the paper were intended to be illustrative, and were not based on any discussions with potential contributors, because we just have not had time. This is something we will need to come back to the Board on.

On the use of resources from the Reserve Account, there were a few questions. Let me just touch on them.

First, there was a question of the impact of the self-sustaining capacity. Just to confirm the projections that we have made so far suggest that if we were to allocate roughly SDR 0.74 billion from the Reserve Account for subsidy resources over the medium term, this would still be consistent with maintaining a self-sustained capacity of about 0.7 billion SDRs per year from 2015, which is broadly in line with the estimates we discussed on previous occasions.

This is a long–term projection, dependent on the assumptions that we make for a number of variables. We mention them in the paper. There was one question about the sensitivity to lower returns on the investment of those resources. The current projections assume that we would get a premium of about 90 basis points from the broadening of the investment authority that is linked to the new income model. If we used the current premium of 50 basis points, the impact on the self–sustaining capacity would be SDR 80 million a year. That is roughly consistent with the numbers we presented early last year.

There is also sensitivity to the interest rates. If interest rates were lower, that would have an effect. We have already built in a lower assumption for interest rates than we had assumed at the time of the new income model. At that point we assumed interest rates would be 5 percent over the medium term. We have now lowered that to 4.5 percent and we also have a gradual path of getting there. So, the interest rate is assumption is more conservative.

Obviously, we will need to look at these sensitivities again in a follow–up paper. If in the end the outcome is different to what we have assumed, so that the self–sustained capacity is lower, we need to look at the options. New bilateral contributions would always be an option at some point in the future, but I think the aim of this exercise would be to agree on a package in which we would have reasonable confidence that we would not need do that for a while. That was also our focus generally in this paper, not just to look at what is needed for the next two years, but to look more broadly, so that we are not faced with a situation where we can support a very high level of lending now but then there is a collapse after two years. We need to look at the medium-term projections and this is consistent with the discussions that Directors have already had in the context of the access paper and the low–income country facilities paper discussion.

One final point on the Reserve Account—I think one of the grays made the important point that it does provide security for lenders to the PRGF–ESF Trust and I can confirm that the projections in the paper are consistent with maintaining what has been the traditional minimum loan coverage ratio, and that is about 40 percent. The Reserve Account should cover about 40 percent of the stock of loans outstanding.

Turning to the gold sales proceeds, a number of Directors said we should keep our options open at this stage. That is what we would intend following up from today's discussion. Obviously there are pros and cons with each of the options in the paper, and I think we need to reflect further on this and come back to the Board.

In terms of the risks for the GRA and how we would cover those, this applies primarily to options 2 and 3. Certainly with option 3, if there is a commitment upfront of a certain amount of resources, then the GRA, as we point out, would take the risk. The key safeguard there would need to be a careful sensitivity analysis of whether the new income model is robust under a range of scenarios. We put a couple of scenarios in the paper, but I think this is something we need to look at more carefully.

There were couple of questions, also, related to option 3, on the gold sales price assumption—what sales price would be needed to ensure residual profits of at least as much as we had projected when the new income model was decided. The new income model assumed a gold sales price of $850 per ounce. In principle, it would be, looking just at the dollar flows, probably over $900 per ounce. I think we calculated it at around $930. However, one additional thing that has changed since the new income model was put together is that the dollar has strengthened against the SDR. This means that in SDR terms, the price in dollars that would be needed would be somewhat lower. The calculations I got this morning were of the order of $840 per ounce that would generate equivalent profits in SDR terms to what we had assumed in the context of the new income model discussions. This is also something we need to look at carefully in the follow-up paper, namely the full implications for the income position.

On what could be done to reimburse the GRA if we found we had insufficient resources under that option—again, there are relatively few possibilities at that point, so the key would be to look at a scenario that is robust to a range of possibilities.

On the question of whether we can pre–finance, what we had in mind in this is that we could only start to use one of these approaches once we had sold at least some of the gold, so that we had some income from that source. That does not mean that we cannot agree on an approach before we have sold the gold. However, that certainly was our initial thinking in the paper. We need to look again more closely at the timing issues here, both the timing of the income stream, and the timing of the needs. Obviously subsidy resources are only needed gradually over time, and in fact we have significant subsidy resources already. We can cover our immediate needs, so the needs are in the future, and one of the second round issues we have not explored yet is the question of timing and how to match the needs with the inflows.

There were a couple of questions on how to minimize the leakage with the distribution mechanism, which would apply in all of these cases.

> Mr. Hagan will pick up on this point, but let me just address Mr. Stein's question and Mr. Rutayisire's question this morning of how this compares with the SCA–1. I think in the case of SCA–1, there was a difference. The contributions that were used for Liberia were members' contributions to the SCA–1, so they were made through the burden sharing mechanism, with a roughly 50 percent distribution between creditors and debtors. The return ratio in that case was roughly two–thirds, so, the leakage was about a third. As we note in the paper, we would expect a lower leakage to be possible in this case given that these resources are owned by the membership and it would be distributed in proportion to quotas. The G–20 members alone account for close to 80 percent of that. Mr. Hagan will pick up on what can be done in terms of the decision.
>
> Just finally on a related question, whether there are internal procedures. I think some countries would have internal procedures. They certainly had them in the case of Liberia. These were funds members had committed, so it may be different in the case of a distribution through a dividend. The information I have is that of the roughly 102 countries that committed resources in the case of Liberia, more than 80 have now disbursed their resources, and roughly 20 are still in the process of completing internal procedures. There may be internal procedures for some countries, and that may mean again that it could take sometime, but probably with this approach, we would have the time.

Mr. Rutayisire pointed out that the Fund would already have approval that a portion of the proceeds from gold sales would go to create an investment fund. He therefore saw no need to pass through the membership in order to have those resources returned to the investment fund.

The General Counsel (Mr. Hagan), in response to comments and questions from Executive Directors, made the following statement:

> There were not many legal questions, but clearly there is some interest in the modalities of using the proceeds of the gold sales for this purpose. The complexity arises from the fact that the gold that will be sold as provided for under the income model, is what we call "post–second amendment gold". This is gold that the Fund acquired after the entry into force of the second amendment. The Articles make it clear, and this is further clarified in the commentary, that any profits that arise from the sale of that gold are assets of the General Resources Account. All of the rules that exist with respect to the use of the GRA come into play. Those rules are, amongst other things, a rule regarding the principle of uniformity of treatment, which is that general

> resources cannot be used to provide assistance to a subset of members on the basis of income. They can be made available for a subset for special balance of payments needs, but not on the basis of income. This is in strict contrast to what we call "pre–second amendment" gold. This is gold that was acquired as the proceeds of subscription. The Articles make specifically clear that profits from that gold can be made available to a subset of members on special terms based on income.
>
> However, the income model assumes that we're talking about post second amendment gold. Since the rules of the GRA apply, the only way in which this can be achieved is if these resources are distributed to the membership, applying the rules that apply to dividends and reserves, and net income, as provided under the Articles, and in accordance with the special majority they require. In that respect, for example, a distribution of dividends requires a 70 percent majority of the total voting power, and then the members would be able to contribute those dividends to the Fund—more specifically to an account administered by the Fund, in this case perhaps the PRGF-ESF Trust, to be administered by the Fund. It would have to go through the membership. Now, how does one avoid leakage in that context? Clearly, there is the precedent of Liberia. It is open to the Board before it makes a decision on dividends to receive the types of assurances that it feels necessary, that members will in fact be willing and able to make that contribution. As Mr. Stein has pointed out, those contributions may indeed involve appropriation actions by the legislatures in those countries because then they become the members' resources.

Mr. Rutayisire said that he did not want to contest the rules of the GRA. But, under the same Articles of Agreement, it was stated that the Fund could create special revenue accounts from the sale of gold. He therefore could not see the connection between the sale of gold and the GRA.

The General Counsel (Mr. Hagan) confirmed that in addition to the GRA, there was a Special Disbursement Account. However, the Special Disbursement Account, under Article V, Section XII, could only receive the proceeds of pre–second amendment gold. That account, with respect to pre–second amendment gold, could indeed provide for the type of operation Mr. Rutayisire envisaged. It had been the basis for the MDRI and the PRGF Subsidy Account. The Reserve Account also contained resources from the Special Disbursement Account. The complexity arose when the income model and the proposed amendment were based on the assumption that the Fund was selling post–second amendment gold, which under the Articles was subject to a different regime.

Mr. Rutayisire pointed out that the Board was meeting to find a solution to a real problem, and he was sure a solution could be found.

The Chairman (Mr. Strauss-Kahn) agreed that a solution needed to be found. However, the Fund's rules were somewhat difficult. The question of selling pre–Second Amendment gold could be reopened, but this would require starting from scratch, rather than building on the new income model. This was the problem with doing the same thing as was done for the MDRI, for example.

Mr. Moser made the following statement:

> On this point, I very much agree with what Mr. Bergo, Mr. El–Khouri, Mr. Kishore and Mr. Kiekens have said. On the point of reopening the gold sales question—to my knowledge, the Board has not yet given the authority to sell the gold. This decision has not been made. The only thing that Directors have given is an indication of their readiness to do so under very specific assumptions, which in my view are not consistent with the latest proposals given here.
>
> It also seems to me a very bad time to weaken the Fund's balance sheet, when we are borrowing and lending as never before.
>
> On the consistency with the income model, I have serious doubts, at least with respect to some of the options that are proposed. When I look again at the report that we had sent to the Board of Governors, and the assumptions of this report under which we had indicated our readiness to vote in favor of a gold sales once this comes to the Board, it was not so much the gold price projections at the center of the focus, it was the clear understanding that all profits from the gold sales will be placed in the investment account and invested. Actually we have even changed the Articles of Agreement to make sure that this will happen.
>
> In our gray, we asked the staff to explain how the proposals, especially option 1 and 3, are supposed to be consistent with the long–standing five principles that we learned from staff, in particular, the principles that any mobilization of gold should avoid weakening the Fund's overall financial position, that the profits from any gold sales should be retained, and that only investment income should be used for purposes that may be agreed upon by Fund members and not permitted by the Articles of Agreement. This does not seem to me to be consistent with at least with option 1 and 3. So if the staff could reply to that, that would be appreciated.

> Just one minor remark on the staff paper: it seems to me that the boundaries of the G–20 are fairly flexible. When I look at the quota share of G–20, it seems to me that there are not just G–20 members in there, but this is a different topic.

Mr. Fayolle reiterated his question about the difference in the average gold price assumed, depending on the options.

Mr. Itam remarked that it would be helpful if the Board could understand better what the G–20 had in mind in terms of the sale of gold and the use of surplus income.

The Chairman (Mr. Strauss-Kahn) made the following statement:

> I will ask staff to answer a couple of questions. I can try to answer the last one. It is very difficult to know what the heads of state have in mind.
>
> I believe that the simple idea was to say that we decided one year ago to have a new income model, but that we will probably have, for a while, some resources coming from lending. Of course those resources coming from lending are temporary resources, cyclical resources, and so we should not jeopardize the income model, because there are likely to be periods in the future where the Fund will be lending less. Meanwhile, we will have extra resources, and those resources could be used to help low–income countries.
>
> One way that would have been easy would have been to go directly and say that the Fund should use some of the resources coming from the additional lending for the PRGF. However, that will hit the same wall that Mr. Hagan was talking about, that the resources coming from lending are GRA resources and cannot be used for some part of the membership defined by income. This way is therefore closed. The other way to do it was to say that money is fungible, so we can go through with the sale of gold, not jeopardizing the income model, and we may use either the windfall gains from the sale, or the extra income from the endowment for this use. In this case, it is not that simple, because as Mr. Hagan just explained, we have to go through the membership to receive this as dividends, which will then give it back to the Fund.
>
> Another problem that has to be taken into consideration is that the sale of gold will happen in the future. It has not been decided by all the parliaments that are interested in giving their vote to this. Then, as Directors know, the sale of gold has to be part of the agreement among central banks. The previous agreement ended last September and a new one is under

discussion, but it still does not exist. Let us imagine that it will come into existence a few months from now. Then we will probably—as was the case for the former agreement—be permitted to sell 80 tons of gold a year for up to five years, of the 500 tons we have to sell. That was the previous agreement and there is no reason to believe it will not be the next agreement. This means that the sale of gold, even if it begins in six months or one year from now, will take a lot of time. So not only the windfall gains from the sale of gold, but also, to an even greater extent, the income from the sale of gold will take time. In reality, the low-income countries need the money now. We are not going to wait for the implementation of the income model or the windfall gains coming from the sale of goal to provide what is needed now.

That is why it is important to know that, as described in the paper, we have enough resources for the two coming years, even if we follow the new path that has been proposed of having US$6 billion available. What is at stake is how we should find the resources for what comes after these two years. Then we come back to something that fits with the sale of gold, if we believe that the sale of gold can begin in six months or one year.

Everything could go well, but it is not that easy, not as easy as political communication from the G–20 to say that we just take the gold and use it for low–income countries. It is slightly more complicated. But we have committed to do something, and we will do it. I think we have two commitments which are compatible. The first one is to provide enough resources to be able to make available loans at a concessional rate. We may discuss the level of concessionality to make available the US$6 billion over the period of time that has been considered. The other is to do this without undermining the income model. I think we can find a way to do it. However, we may challenge the point that everything that is written in the staff paper is coherent and consistent with the income model, although the income model is something we have to respect. The other thing is that we have to provide the resources. US$6 billion will be a significant sum. I do not have the exact figure at hand, but since the beginning of this year, we disbursed something like a few hundred million. This means that US$6 billion is really a huge increase, and hopefully we can use it. I am not even sure that we will not have excess resources and that it will be possible to use such an amount.

However, we are going to work towards this target. I think the discussion this morning has been useful so far because it is a complicated area, so we have to discuss it, come back, there is no way to be in a rush. We can discuss this again soon after the Spring Meetings and then have a third meeting, and, if necessary, a fourth meeting, until we find the right way to do it.

Mr. Rutayisire remarked that the timing of the sale of gold would not matter if the proposal of the U.S. chair could be adopted, by anticipating the receipts that the Fund would get from the gold sales and allocating resources to the Subsidy Account on that basis. The constraint was on defining which gold could be sold. If any gold could be sold, then that constraint could be resolved.

The Chairman (Mr. Strauss-Kahn) agreed that the Fund had to anticipate the resources from the gold sales, by finding funds from other sources, because the resources were needed as soon as possible.

Mr. Kiekens made the following statement:

> Some Directors have become very polite the last few days. Following their example, I respectfully disagree with the chairman. I do not agree that all that is in the staff paper is consistent with a good faith or a strict interpretation of the income model. I do not agree that this meeting was useful. My impression is that it has created more confusion than is necessary.
>
> We should have a clear view—the sooner, the better.
>
> My impression, listening to this Board, is that this institution is without a credible guardian for protecting the financial integrity of the institution. My impression is that the Fund risks being used as a scheme to extort from middle–income countries monies that advanced country leaders are not willing to pay up or face themselves, even if they want to show strong generosity to the poor countries vis–à–vis the world of public opinion.
>
> We have a very balanced solution. Half of the SDR 1.5 billion is proposed to come from the resources of the Fund. I have tentatively agreed with that on condition that the staff provides me, with more detailed calculations. We use about SDR 750 million from the Reserve Account, which as Mr. Hagan rightly said, are monies from the Special Disbursement Account, which are monies that indeed are reserved for financing and subsidizing low–income countries. I agree with that, but I regret that my written request for having more detailed calculations has not been followed up on yet. I hope that the chair can instruct the staff to give me the written calculations.

Second, the other SDR 750 million must come from contributions by donors. There is no way around it, and that is what we have to agree.

The only complication is that it is not clear when donors can expect to receive dividends. There is no legal link between their donations and dividends and they should not link it.

My view is crystal clear on that. We can pay out dividends when we have profits or when we have excess reserves. Do we have profits? And excess reserves? No. Absolutely not.

Before that, can we use the capital gains from gold? The answer is crystal clear. No. I think it is very clear in our decision. All the capital proceeds from gold must be in the gold endowment and the gold endowment is not available for distribution. What is available is income. However, our income is dropping like a stone, at least income that we will have and that we receive from our reserves.

Last year, income was projected at SDR 345 million. For the next fiscal year, and the fiscal year thereafter, assuming an SDR rate double of the one which is now, it is US$ 83 million. Of course, we will receive surcharges, and we receive charges. But, it has been decided by the Board very clearly that these resources will go towards building up precautionary reserves, in order to reach the target. We all agree that, unless we have reached the target, there is no way of paying out dividends. That was clearly said by Mr. Talbot and Mr. Hills in their statement on December 5, 2008. "We agree with staff that reserves in excess of the target level should be redistributed to members via dividends—but only for the market risk pool. We would argue that those accumulated in the credit risk pool should be redistributed in the form of a reduction in the rate of charge—and not by continuing to ask for excessive rates of charge and surcharges when we have excess reserves."

When we agree on an income model, we need to adhere in good faith and in a strict sense to what we have agreed. If not, we cannot proceed further. Mr. Moser was very to the point. We have not yet taken a decision on gold sales. We need to have a good understanding as to what our dividend policies will be before we decide on gold. I hope we can agree.

I have made a very clear proposal and I repeat it here today: make up a list of all the countries to be invited to contribute and give a range of what we expect them to contribute, make that list public. The success of a Managing

Director depends on his ability to raise money for the poor. I expect the chair will do that, and I support him for that.

The Chairman (Mr. Strauss-Kahn) made the following statement:

The point is that there are some legal questions that are interesting and which we may discuss in the Board. But, there is a limit to the legal questions. The limit to the legal question is what the membership decides to do. The membership may decide to change the legal framework in which we work. A large part of our membership has decided, rightly or wrongly, that we should use our gold reserves. Some members may be against this idea. We may need to find a way to do it that is compatible and consistent with the income model. However, at the end of the day I find it very difficult for this Board to oppose what a group of world leaders have decided, when they represent 80 percent of the voting power in the Fund. Sometimes we may believe that what has been decided was decided too soon, because it is more difficult than it appears, for other reasons that have been discussed this morning. So, that is why we need to find a way to be in line with what has been asked of us by those who represent our members. At the same time, we need to do it in a way that does not compromise the future of the institution. But that is why it is difficult.

I do not believe that the discussion this morning adds more confusion. It depends on who you ask. At least for me it has been enlightening, but I do believe we are not at the end of this discussion. Mr. Kiekens is right in saying that there are many points that still need to be discussed. I still believe that it is possible to find something that responds to the request by a large part of our membership and on the other hand does not jeopardize what we built last year as far as the income model is concerned. I do believe it is possible, but of course it needs everybody to make some efforts. If not, there is a risk of having this income model forgotten. This risk should not be underestimated. I was very happy to hear from Ms. Lundsager that she believes that the U.S. Congress will vote in favor of what we need for the income model. This means that at one point in time it will be voted on, but we are never sure. Until this has been voted on by most legislatures, including the U.S. Congress, we are not even sure that this income model will survive. We are in a difficult situation, because we want to build on something that is not yet completely finished. We need approval by the legislatures—a vote by the Board and even by the membership is not enough. At the same time, we have a commitment by the heads of state of the G–20, and if we believe it is somewhat important, we have to find a way to follow this indication. I am not sure that only legalistic considerations may solve the problem. We need to have a more political view of what is at stake, and I am sure that all Directors have that in mind when they write their grays and make their proposals.

Mr. Kiekens made the following statement:

The Chair is absolutely right that with the proper procedures and decisions, the Articles of Agreement can be changed. However, it is not my understanding that the G–20 asks us to consider solutions that require changing the existing legal framework. My understanding is that the invitation to us is to honestly examine how we could be helpful within the given legal system. I do not read the communiqué as a commitment by the leaders. They have simply asked us to give an opinion on what can be done. My opinion is clear. Dividends can be paid under the conditions that dividends can be paid. There is no real particular perspective in my opinion that dividends will be paid. We can agree or disagree with that, but that is the exact issue that should be discussed.

We can discuss, as Ms. Lundsager says, whether we can give grants and more concessional loans. But, that is not the topic. The topic is, where is the income coming from? I am very disappointed to see that an important shareholder like Ms. Lundsager tells us that we should give grants without providing a precise proposal of how we are going to finance that. There is a straightforward proposal, but that is not on the table today. That is, change the Articles of Agreement, decide on more gold sales, and do what we did before the second amendment, by making it clear that the income is for poor countries. However, it is difficult to reconcile that with the need for emerging market countries to pay very high premiums in order to build up precautionary reserves, that the same G–20 leaders want us to build up even faster than we are already doing. That is the inconsistency and the problem we need to solve.

SDR 750 million to be paid over the next seven years is a very small amount compared to what this Board decides emerging market countries should pay. I am astonished that there is not more willingness to pay that small amount in terms of contributions.

The Chairman (Mr. Strauss-Kahn) made the following statement:

Mr. Kiekens is right in saying that the right way and the easiest way to do it is to change the Articles of Agreement.

The answer is, it is not exactly my impression that what the G–20 had in mind was just to ask us if we could find a general way to help them. The

> discussions were difficult. I mentioned that I fought several hours to have included in this sentence the phrase "consistent with the income model," because the first proposal did not include this at all. Nobody had it in mind that it was important to maintain the income model. That was the fight I had, and I think I won on the Board's behalf, and I assume I had your support for this. Now we have a position which is not that bad, because we have to be imaginative enough to do what we need to do to help our low–income members. I am committed to doing that, but in a way that is consistent. I will ask FIN to provide Mr. Kiekens with the figures he asks for. The questions on the substance, whether the proposals on the table are consistent or not, is a very important discussion.
>
> I do believe that they are consistent. Perhaps I am wrong. Mr. Kiekens will have to prove the contrary, if he is right. But, if he is right, then we have to find other ways. What is sure is that we will not provide solutions that are not consistent with the income model. Of course, the easiest solution will be to raise some subsidies. But, I am afraid that it will take plenty of time, and it will not be easy in the current circumstances to have this money coming from our shareholders.

Mr. Kiekens recalled that a few months earlier the Board had decided that if the subsidy resources in the PRGF-ESF Trust were not enough, the first thing the Fund would need to do would be to address itself to the membership in order to raise money. He expected that countries, when they received dividends, would to a large extent use them to contribute to the PRGF-ESF Trust. However, this could be at the expense of additional bilateral contributions. The Fund would have no influence on those decisions and he therefore found the scheme to be a cynical one.

Mr. Gibbs made the following statement:

> I just wanted to make a few points additional to my gray and following the discussion. First, I would like to thank the staff for responding so quickly to the G–20 request.
>
> Secondly, I would note that the circumstances are exceptional. I agree with everything the staff has said about the complexity of the legal issues and the complexity of the financing issues. However, when we are discussing what it is that the G–20 asked us to do, it is important to reflect on the exceptional circumstances, which are, for the low–income countries, an exceptional need to potentially draw on the PRGF over the next two to three years, and for the donors that have traditionally financed it, exceptional budgetary pressures. Of course, at the same time, the crisis that has caused

these circumstances has had a different impact on the potential lending income of this institution. It seems to me that the G–20 was reflecting those circumstances, and I believe they were doing more than asking us for an opinion. They were committing to support action in the near term that gives certainty to the Fund's most vulnerable members, that the Fund will be able to respond to their needs. I would personally want do nothing to discourage the Fund’s efforts to increase donor resources. I think that we do need to try to develop a fully financed package that frankly reflects the financial realities. Option 3 gives us a basis to do that, and that is why I supported it in my gray. But we need to look again at the assumptions about potential donors— it rests a little too heavily on that, in my view. This is a preliminary discussion, and the options will be worked out and the projections underlying them refined. I look forward to the next iteration.

While I have the floor, I would like to echo two comments that colleagues have made.

Ms. Lundsager put some ideas on the table for increasing the concessionality of the PRGF. I am certainly open to considering that. I would encourage the staff to look at all potential aspects of concessionality, including grants but also the other concessional terms. I think these ideas deserve consideration.

Finally, my position on reimbursement of the GRA is identical to that expressed by Mr. Fayolle. I did not comment on this in my gray, but I think it would be very hard for us to start triggering this reimbursement at the time the PRGF-ESF Trust is potentially in most need of resources.

Mr. Lushin made the following statement:

It is not an easy task, but I would like to talk about some practical issues. In order to accommodate the G–20 commitment, we need to understand what it actually means, and, in my gray, I tried to do this. It seems to me that the staff proposal put forward in the paper goes somewhat beyond what the G–20 requested from the Fund, above the two to three years horizon and mobilizing subsidy resources up until 2015.

Mr. Tweedie explained why this happened, because we may not want to face a situation when large disbursements in the next two to three years, which are in line with what G-20 commitment says, are followed by a much lower capacity to provide concessional financing after 2011. This is understandable. But this assumption of a sudden decrease in concessional lending after 2011 implies that no further donor contributions are forthcoming, and the Fund has to take care of the subsidy element not only during the two to three years requested by the G–20, but up to 2015. I am not sure that we should think that donor resources are gone forever. There is definite difficulty with mobilization of donor resources during the crisis. But, following the crisis, we could reasonably assume that more financing for subsidization will be feasible. If so, the amount that is required from the Fund to contribute to accommodate the G-20 proposal would be, in my own calculations, half as much as that proposed by the staff, and correspondingly presenting much less risk for the Fund's new income model.

Mr. Kiekens made the following statement:

Mr. Gibbs says that the situation is so exceptional that we need to do something exceptional. I would like to remind him that the situation is exceptional not only for advanced countries, but also for emerging market countries. Their fiscal situation is probably affected to an even greater extent than the fiscal situation of advanced countries. At least what they have to pay as a share of their budget to the Fund is immensely more important than the small contribution that I expect from them.

But, that being said, Mr. Gibbs's alternate had a very clear interpretation as to when dividends should be paid only a few weeks ago. The situation was then equally exceptional as it is now. There is a solution, and I have mentioned that in my statement. We do not need advanced countries to pay contributions this year and next year. What we need are credible pledges that they will be able to pay contributions later when their fiscal situations should have improved. I have offered an avenue to say, let us, on the basis of these credible pledges—for payments in the outer years, not now—bridge the financing by transferring monies from the Special Disbursement Account that are in the Reserve Account. Of course, this will result, to some extent, in a weakening of the guarantee that we give to lenders and we need to see whether we can agree with that. However, I think that is a good solution. All the arguments that the fiscal situation is now very difficult can be addressed by saying to ministers that they should commit a very small amount of money, a couple of million, a couple of tens of millions, to be paid in the next few years. Make the calculation and then publish it, and make sure to communicate to NGOs and the world public opinion what it is we exactly are asking and not asking for. We need to have at least the courage to be clear on what we ask for.

Mr. Legg made the following statement:

> I have a lot of sympathy with the way Mr. Gibbs saw the issue in front of us, and I want to say I very much support and appreciate the Chair's efforts to protect the income model. I think the Chair's work to keep that framework in the forefront of the communiqué is very much appreciated. Like the staff, we have to have a pragmatic approach to squaring this particular circle.
>
> I entirely agree that the first focus should be on getting whatever one can out of bilateral donors and I agree one should take a long-term view on that, but I think option 3 provides the pragmatic safety net, for the decisions we need to take now. The problem with option 3 is that it leaves the risk being borne by the GRA, and Mr. Tweedie talked about managing that through sensitivity analysis to see just how far we can push that. I welcome that. But, I think in our gray, we also raise the possibility of trying to limit that risk by taking a decision now that beyond a certain point we would stand ready to make the GRA whole again if assumptions did not work out. I think some mechanism for limiting that arrival risk would also help maintain the pragmatism as well as the principle of income model.

Mr. Gibbs noted that Mr. Kiekens had correctly reminded the Board of the position taken by his chair before the latest set of meetings, in December 2008. However, the world had moved on and political leaders had made commitments, including the British Prime Minister, and his chair had no problem reflecting those commitments in its positions.

Mr. Kiekens expressed the view that Directors that had to act on instruction of their authorities, where there was a conflict of interest with that of the Fund, should abstain from participating in the decision.

Mr. Nogueira Batista made the following statement:

> I think the G–20 and other fora are at their best when they build upon discussions at institutions like this one, other international institutions, and when they work at the deputies level, and through working groups they establish in the preparations for their meetings. The G–20 and other such fora may create complications when they act on the spur of the moment. I was in the G–20 working group on the IMF, as Mr. Lushin also was. We have held intensive discussions since January 2009, and this proposal never came up in the working group. This proposal, which was modified by the Managing Director's efforts, came up something like 10 days or one week before the summit. Then, the Managing Director had to do some damage control by

introducing "consistent with the new income model", because this is a very difficult situation.

The proposal sounds marvelous—those bureaucrats in Washington are sitting on a pile of gold and, with millions starving, let us take the gold, sell it, and use it to support the starving millions. It is very different when one comes to a proposal after a long build up, as was the case with the income model. I think the intention of the G–20 leaders was to indicate the priority of giving financial support to low–income countries. But if they have come up with something that is inconsistent with the new income model, I am anxious to hear the replies from staff to the question from Mr. Moser. Are the options really consistent with the new income model? If they are not, the paragraph is inconsistent. We therefore would have to reach the objective of providing US$ 6 billion additional financing over the next two to three years through another route, a route that is consistent with the income model, and that may not be necessarily based in the exact detailed drafting of the paragraph. The spirit is to provide the resources over the next three years. I do not know if it helps saying this, but maybe we should listen to what the staff has to say about the consistency problems that were brought up by Mr. Moser and also by Mr. Kiekens.

The Director of the Finance Department (Mr. Tweedie), in response to additional comments and questions by Executive Directors, made the following further statement:

I apologize for not addressing Mr. Fayolle's question in the first round. I had meant to.

The $810 per ounce assumption in footnote 13 is the current two–year average of the gold price. This is the price that we have used in the income papers, the medium-term projections, and also the income paper for FY 09 and FY 10. We have updated the original income model, which was based on $850 and I think in the December 2008 update, we used the two years moving average, and we have done it again this time. It is an assumption, but it is the price we are using in all the calculations we presented in these papers.

The broader issue is whether that is consistent with the new income model. When the income model was put together, it assumed certain policy actions and decisions, and it was based on assumptions that were made at the time that showed it met its objectives, a sustainable income position over the medium term. Under the income model, the Fund would have a broader range of income sources than it has had in the past, when it has had to rely mainly on income from lending. The margin for the rate of charge could move once the income model is in place, to covering intermediation costs and reserve buildup. So those are what we saw at main elements. The calculation that the Board had at the time when it agreed on the new income model showed that this worked, based on the assumptions made at the time, including the payout from the broadened investment mandate, where we issued the 3 percent payouts and showed sensitivities at that time.

However, what has happened in the last year is that prices, exchange rates and interest rates have changed. Also, the Fund is now lending in a substantial way again which was not assumed in the new income model .The approach we took in this paper was to ask, if part of the gold proceeds were to be diverted for the provision of subsidies for concessional lending, would the income model still be intact? We looked at that from the perspective of whether the broad range of elements would still be in place, which means the gold endowment, and the broader sources of income. Based on the preliminary numbers we have so far, we think it does. Obviously we need to come back to this.

Then we looked at the different options. Mr. Moser is right, that in only one of the options would the corpus be preserved, and for the other two we would use either a windfall profit from what was assumed previously, or set aside a certain amount. So, the option 2 would be certainly the most consistent with the fifth principle of the Fund's five principles on gold. I would just make two comments on that.

On the financial implications, while it is true that preserving the corpus is important, the financial implications overall of using some of the income, when we get beyond this period, should be broadly the same in terms of how much is diverted through a provision of subsidy resources. The other point I would make is that the Board has diverted from principle five in the past. The most recent occasion was the decision on the MDRI, when the corpus from earlier gold sales proceeds was used. I think that is one of the considerations the Board will need to take into account in looking at these options.

The General Counsel (Mr. Hagan), in response to additional comments and questions from Executive Directors, made the following further statement:

I think it is important to make a distinction between the concept of consistency with the income model and consistency with the legal framework under the Articles of Agreement. It is very important, as Mr. Tweedie has pointed out, to note that the income model as stated first in the Crockett report, it was then somewhat revised by the staff in subsequent reports. The concept of flexibility was introduced, the fact that we needed to have some flexibility in the margin to deal with changing circumstances. The new income model was based on certain financial assumptions, and I think the point Mr. Tweedie is making is that organic flexibility does provide some room for this. That is separate from the Articles of Agreement. It is really important to make the point that none of the options are inconsistent with either the existing Articles or the proposed amendment. More specifically, there is nothing in the Articles that constrains the capacity of the Executive Board by a 70 percent majority of the total voting power from distributing reserves as dividends.

The Board may adopt a policy saying that we are only going to distribute reserves and dividends at a certain point, but it can change that policy. The Articles do not constrain the discretion of the Board to distribute reserves as dividends, as long as there are reserves.

The Board may tie its own hands, but then it may change those rules.

Mr. Kiekens agreed with Mr. Hagan's intervention, but disagreed with Mr. Tweedie's response to Mr. Moser in respect of the fifth principle. To preserve the corpus of the gold sales would be a legal requirement under the Articles of Agreement. It was not true that the Board had deviated from principle five in the past. It was the Articles of Agreement that had allowed the use of capital gains from the sale of pre-Second Amendment gold for subsidizing low–income countries. A new amendment of the Articles of Agreement would be required to use the corpus of the gold sales to subsidize low–income countries. But the requirement of "consistent with the new income model" requires a good faith interpretation of what Directors had in mind when it was agreed on, which included that surcharges were necessary to build up precautionary reserves. Payment of dividends would be doing just the opposite, and it would not be consistent.

Mr. Fayolle remarked that he was still unclear on how the average gold price had been chosen. If the most recent two year moving average was $810, he was not sure why it was $850 at the time when the income model was agreed upon. It should have been below $810.

The Director of the Finance Department (Mr. Tweedie) clarified that different approaches had been used at different times. At the time of the income model discussion, a two–year average had been used at one point. However, a number of Directors had had the view that that was out of date, given the steep rise in the price of gold, and had asked the staff to use a more current price. That price had been used in the final calculations for the income model. The staff had then had to decide how to update those projections every few months for the Board. Some Directors had requested that the staff use a forward–looking price, but what tended to happen was that the forward–looking price in the gold market was very much linked to the current price. For the previous two papers, a backward–looking model had been adopted, taking the average price over the last two years. This was not necessarily a good predictor of the future price, but a similar problem arose with all the assumptions that could be used.

Mr. Kiekens argued that it was not useful to make assumptions on gold prices. There was a clear correlation between interest rates and gold prices and, even if gold prices were high, interest rates were low, with the consequence that the income from the Fund's investments and reserves was dropping dramatically. The most relevant parameter was the dramatic drop in interest rates. Income from the Fund's precautionary reserves was already much lower than the year before, at US$ 345 million, and next year it was projected to be only US$ 83 million.

The Chairman (Mr. Strauss-Kahn) made the following statement:

> Certainly, everybody wants to maintain the income model and to act in a way that will not undermine it. It is not clear what it means to undermine the income model. In my view, the income model stands as long as the endowment exists, no matter what we do with the income from this endowment. We can postpone the moment that the income model comes into effect, but what we cannot do is to make it impossible to work because we do not have the endowment. The most important thing in my view is to avoid the income model being destroyed by the disappearance of the endowment.
>
> What we can do is use any windfall. However, it is difficult to know what the windfall is because it refers to the normal price we had in this model and the price is moving, as Mr. Fayolle rightly noticed.
>
> On the other hand, I think the G–20 may have had in mind exactly what Mr. Nogueira Batista said: to use the endowment from the gold sales. What the heads of state understood by "consistency with the income model" is that the endowment after the sale of gold should be maintained, meaning that the income model can be implemented at some point in time, even if not immediately, because the income will be used for something different.
>
> With the solution, we should find a way on the one hand to provide the US$ 6 billion, to provide the necessary subsidies, including by looking at the pledges we may have from different countries, and we already have some. Some members have already made some pledges to increase our capacity for concessional lending. Of course, it is not enough. So, we need to find a way to

provide the US$ 6 billion, at a level of concessionality that still has to be discussed.

On the other hand, we should not put ourselves in a situation where it would be impossible to establish the income model, because the resources to do so had disappeared. It is simple to say it that way. However, it is very difficult to define concrete proposals because there are a many assumptions behind this, and many ways to do it in good faith, as Mr. Kiekens said. This includes the level of precautionary balances, which everybody agrees should be increased. But there is no magic trick to decide on the right level. The point is that we need to find a solution here, and we need to find a constructive way to discuss it together.

My proposal is that we take a few days to think about this and discuss the issue further after the 2009 IMF/World Bank Spring Meetings. We should discuss this in a very informal way, trying to see exactly what the constraints are and how we can find a solution which fits with everything. I think it is possible, including trying to raise more funds from the membership. Some will agree, some will not, but it is part of the job being done, at the end of the day, to be able to solve this question, and to provide our low-income members with the resources we are committed to providing. At the same time we would need to make it possible for the Fund to continue with the income model.

What I would propose is to write a very carefully crafted summing up that we could read tomorrow. Following that, we would convene a new meeting, as soon as possible after the Spring Meetings, to discuss this informally. Alternatively, if we do not have a new proposal at that time, we could postpone the meeting for a week, and see what kind of proposals are likely to take into account most of the remarks that have been made today. It would be a difficult exercise. Hence, the quicker we go, the better.

Mr. Kiekens pointed out that half of the resources needed were coming from the Fund already, while the other half was also pre–financed by the Fund. What countries needed to finance, they would need to finance anyway, and dividends would be paid whenever resources were available. He believed that the Fund was very close to what would be a very manageable solution.

The Chairman (Mr. Strauss-Kahn) said that was one possible route, although it was not certain that it would work. However, it was necessary to find a solution to deliver.

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G. RUSSELL KINCAID
Acting Secretary