

**FOR
AGENDA**

EB/CQuota/10/2
Correction 2

April 12, 2010

To: Members of the Committee of the Whole on Review of Quotas

From: The Acting Secretary

Subject: **Fourteenth General Review of Quotas—The Size of the Fund—Initial Considerations**

The attached correction to EB/CQuota/10/2 (3/15/10) has been provided by the staff:

Factual Error Not Affecting the Presentation of Staff's Analysis or Views

Page 12, footnote 16: for “In the current global crisis, exits from the FTP have been limited to Hungary, but in previous crises, such as the Asian crisis, there was a larger reduction in the size of resources available through the FTP.”

read “In the current global crisis, exits from the FTP have been limited to Hungary and Kazakhstan, but in previous crises, such as the Asian crisis, there was a larger reduction in the size of resources available through the FTP.”

Questions may be referred to Mr. Beaumont, FIN (ext. 37411).

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

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14. **The expanded NAB would replace this bilateral financing with a larger backstop to quota resources.** Standing borrowing arrangements have long been used by the Fund to provide a multilateral framework for supplementing its quota resources (Annex I). However, the NAB was not activated in the current crisis as it was too small to provide a credible boost to Fund resources. In addition to being expanded from SDR 34 billion to about SDR 367 billion, it is intended that the reformed NAB will be a more flexible tool for crisis management than the current NAB (Box 1).¹³ The fundamental backstop character would remain unchanged, with the NAB only to be activated when supplementary resources to quota resources are needed in order to forestall or cope with an impairment of the international monetary system. (Annex II compares key features of quotas with the proposed NAB.)

Box 1. Key Elements of the Proposed NAB Reform

The NAB is being reformed to make it a more effective tool of crisis management, while safeguarding the participants' interests. Key reform elements are:

- **Expanded range of allowed uses.** The current NAB is available only for specific transactions, which vary between participants and non-participants, and cannot, e.g., be used to finance FCL arrangements. Resources of the expanded NAB will be available to finance all GRA transactions by NAB participants and non-participants alike.
- **More operationally flexible form of activation.** To provide increased operational flexibility while ensuring appropriate governance of NAB resources, the cumbersome procedures for activation on a loan-by-loan basis are to be replaced by “periodic” activation, where NAB participants would authorize the use of NAB resources for arrangements approved, or outright purchases made, during a certain period (of no more than 6 months), up to a limit which could be below the total credit arrangement. Within such authorization, the use of NAB resources would be decided by the Executive Board through quarterly resource management plans.
- **Strengthening the built-in liquidity buffer for possible early repayments.** The NAB will include a stronger framework for using NAB resources to finance possible early repayments to a NAB participant with a balance of payments need. This will allow all NAB claims to continue to be treated as reserve assets regardless of their size. It will also reduce the need to maintain a liquidity buffer of quota resources, thus allowing the Fund to commit a larger share of quota resources before the activation of the NAB would need to be considered, reinforcing the backstop nature of the NAB.
- **More flexibility in admitting new participants and in increasing the size of the NAB.** The NAB will be modified to allow admission of new participants at any time (currently this is possible only when the decision is reviewed, unless it is amended by an 85 percent majority).

¹³ Amendments to the NAB are discussed in the forthcoming paper, *Proposed Decision to Modify the New Arrangements to Borrow*.

15. **The foregoing indicates that quota resources should at least be sufficient to meet members' needs in most circumstances.** As discussed, Fund practice and policy has been to borrow principally in circumstances where a temporary supplement to quotas is necessary. In addition to being temporary, recourse to borrowing should be exceptional:

- ***Given the voluntary nature of bilateral borrowing, its availability is not assured.*** Maintaining quotas at a level such that recourse to borrowing could be reasonably anticipated would therefore unduly risk undermining confidence that adequate Fund resources are available when needed.
- ***NAB resources are accessible only when the activation conditions are met.*** Activation has a separate governance structure that requires approval by a super-majority of the subset of Fund members that participate in the NAB.¹⁴ Moreover, while the NAB is a standing borrowing arrangement, it is subject to regular reviews, and the size of the NAB shall be reconsidered in light of the outcome of the 14th General Review.¹⁵

16. **Nonetheless, by back-stopping quota resources in case of threats to international financial stability, a standing NAB provides important support to the Fund's quota based financing mechanism.** A sufficiently large standing NAB gives confidence that adequate resources will be available in the exceptional circumstances that warrant activation. Hence, while additional quotas over those needed in most circumstances would help provide assurance regarding the immediate availability of resources, quotas need not be as large as would be necessary to fully cover such "tail risks". During a severe crisis, demand for Fund arrangements is likely to originate from members that had access to international capital markets, including from some members in the FTP. A large NAB can credibly commit substantial resources to such members, helping to limit exits of members from the FTP and the associated reduction in the Fund's available quota resources.¹⁶ The built-in liquidity buffer in the reformed NAB also implies that the Fund can use a larger share of its quota resources before the NAB needs to be activated compared with bilateral borrowing.

¹⁴ Activation of the NAB would follow a proposal for the establishment of an activation period from the Managing Director summarizing the need for a temporary supplement to the Fund's resources in order to forestall or cope with an impairment of the international monetary system. Activation would require first the approval by NAB participants holding 85 percent (increased from 80 percent in the existing NAB) of credit arrangements eligible to vote, and then a decision by the Executive Board by a majority of the votes cast.

¹⁵ It is proposed that the amended NAB be reviewed no later than November 15, 2011.

¹⁶ In the current global crisis, exits from the FTP have been limited to Hungary and Kazakhstan, but in previous crises, such as the Asian crisis, there was a larger reduction in the size of resources available through the FTP. An exit from the FTP would also reduce NAB resources if the member participates in the NAB, as members that are no longer in a sufficiently strong external position to participate in the FTP would not be subject to calls under the NAB.