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October 27, 2020

Statement by Mr. White, Ms. Johnson, and Mr. Yoo on Review of the Adequacy of the Fund's Precautionary Balances
(Preliminary)
Executive Board Meeting
October 30, 2020

Increased lending as a result of the Fund's response to the COVID pandemic has intensified credit risks and other associated risks to the Fund's balance sheet. Credit outstanding is around the same level now as the peak following the GFC, with much higher levels of emergency financing and significant lending concentration. In considering concentration risk, care should be taken to differentiate between credit outstanding – particularly Argentina's large repurchases falling due in FY2023-24 – and committed but undrawn resources: we remain of the view that in most circumstances the use of precautionary arrangements reduces the probability that a country will need to draw on Fund resources and this should be considered when exercising judgement under the framework. We continue to advocate for the 2022 review of precautionary facilities to consider the scope for flexibility in scoring of precautionary arrangements in the FCC.

Given increasing risks, we agree that the indicative medium-term target for precautionary balances should be increased to SDR 25 billion. We consider that the rules-based framework remains a useful guide for assessing precautionary balances and continue to support the view that judgement and Board discretion remain an important part of the framework. On balance, we support staff's proposal and analysis under the framework. But the potential downside risks point to the need for ongoing monitoring and, if warranted, staff should come to the Board with carefully considered options to adjust the pace of accumulation of precautionary balances or the medium-term target, in the broader context of the Fund's income.

We agree with the proposal to maintain the minimum floor for precautionary balances at SDR 15 billion. The minimum floor should continue to be calibrated to ensure the Fund maintains a sustainable income position, as well as to address an unexpected rise in credit in the future, noting Fund credit can be highly volatile and increase sharply with little notice while precautionary balances are slow to accumulate.

Looking ahead, given the significant uncertainty we ask that staff complete the regular review of the adequacy of the Fund's precautionary balances as needed but no later than within 12 months. An adequate level of precautionary balances is an integral part of the Fund's overall strategy for managing financial risks and ensuring balance sheet resilience. The adequacy of the Fund's precautionary balances should remain a critical part of the Fund's risk mitigation framework and this is particularly important given the risks emerging over the medium-term. We look forward to the opportunity to consider staff options on the role and level of balances in the SCA-1 following Sudan's arrears clearance.