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**Statement by Mr. Guerra and Ms. Arevalo Arroyo on Review of the Adequacy of the
Fund's Precautionary Balances
(Preliminary)
Executive Board Meeting
October 30, 2020**

We want to thank staff for the comprehensive report on the review of the adequacy of the Fund's precautionary balances.

While credit and financial risks, compounded by the COVID-19 shock, have increased since the last review, we have a different view related to the current regional exposure of the Fund and how precautionary arrangements are being accounted. First, while regional concentration has shifted to the Western Hemisphere at around 43 percent of total Fund credit outstanding, we underscore this is roughly half of the peak concentration by region in comparison to other reviews. Moreover, even when exposure is accounted on a commitment basis, the current concentration in the Western Hemisphere is significantly lower than in different regions in other years. In this regard, care should be taken to differentiate between credit outstanding and committed but undrawn resources. We consider that full scoring of precautionary arrangements to determine concentration risk is misleading. Besides, we emphasize our view that precautionary instruments contribute to a reduction of risks for the IMF: precautionary program requests entail engaging with the Fund in a timely manner – both locally and regionally –, send a strong signal to the markets, provide an effective insurance mechanism and diminish the impact of negative spillovers within regions.

We consider the current precautionary balances assessment framework adequate.

Notwithstanding the current context of extreme uncertainty, with implications for both demand of Fund resources and income volatility, the framework provides sufficient guidance for the Executive Board to make well-informed decisions. At this stage, we do not believe

changes to the framework are warranted. However, we do believe there is scope for staff to study the feasibility of carrying out joint periodic reviews, disaggregated by type of reserves, considering varying purpose, endowment and hypothetical distribution of the three components that make up precautionary balances. The review of SCA-1 is particularly relevant for the foreseeable settlement of arrears and debt relief of Sudan in the future. *In staff's view, what are the potential implications of low-for-longer interest rates on the precautionary balances framework?*

We support staff's proposal to increase the indicative medium-term target for precautionary balances to SDR 25 billion and keep it under close review. We agree with staff this is warranted as the baseline scenario on demand for Fund resources is expected to increase in light of the pandemic. The Executive Board should continue to monitor developments and be mindful that given persisting uncertainty, the medium-term target could be revised if deemed necessary and in case of major rise in demand for Fund resources, **We also support the staff proposal to maintain the minimum floor for precautionary balances at SDR 15 billion.**

Although there is inherent volatility in the IMF's income, the average pace of reserve accumulation in the last years has been adequate. Thus, at this juncture, we do not see a need to take additional action to increase the pace of accumulation, even if the target is raised. Under a scenario of increased lending by the IMF in response to the current multidimensional crisis (COVID-19, commodities, financial markets), there will be a corresponding increase in the Fund's income stream and, therefore, a higher pace of accumulation of reserves in the medium-term. Regarding income volatility, we understand it is mostly driven by IAS-19 pension-related adjustments. We wonder whether something else could be done to minimize such volatility. *Staff's comments are welcome.*

Finally, we want to draw attention to the stress being placed on the IMF's burden sharing capacity by the lack of agreement to increase quota resources. In our view, this is an important element to take into consideration when the Executive Board discusses the sources of financing for the SCA-1 in due course. In case of a need to reassess the target before the next regular review, this Chair would call for the Board to reevaluate if the IMF is adequately resourced to face the post-COVID-19 demand. This should include an assessment of the resources structure and the need to have a fully quota-based resource envelope. *Taking into consideration WEO scenarios and the possible use of NAB resources, could staff comment on the difference between a quota-only resource envelope vs. the current*

composition of total resources related to the precautionary balance model (including on burden-sharing capacity under the assumption that all NAB resources are used)?