

CHAPTER 3

The Evolution of the IMF's Policies with Respect to Prolonged Use of Its Resources

1. This chapter describes how the IMF's policies with respect to prolonged use have evolved over time. It shows that these policies have moved gradually toward greater acceptance of the need to finance adjustment over a longer time period, especially in low-income countries, and that this has increased the probability of prolonged use. However, the implications of some of these changes both for the extent of prolonged use and possible adverse consequences may not have been fully and explicitly recognized. It also describes how some elements of a strategy for dealing with prolonged use were adopted by the IMF's Executive Board at various times; however, the country case studies and other evidence suggest that these strategies were not fully implemented.¹

Evolution of the IMF's View of Prolonged Use

Prolonged use of the IMF's general resources

2. The official interpretation of the mandate of the IMF was initially unambiguous on the temporary nature of its assistance, and policies on the use of Fund resources (UFR) reflected that interpretation. However, in the 1970s it became clear that even difficulties of a "temporary" nature could require a lengthy period of adjustment and this led in 1974 to the decision to create the Extended Fund Facility (EFF). Although the EFF recognized the need for a longer adjustment period, it was nevertheless expected that the economic program supported by an extended arrangement should be "adequate for the *solution* of the member's problem."² A further step was taken in 1981, with the institution of the enlarged access pol-

icy (EAP). This policy was intended to help members address balance of payments problems whose solution required "a relatively long period of adjustment and a maximum period for repurchase longer than the three to five years under the credit tranche policies."³

3. The creation of concessional facilities (the SAF in 1986 and the ESAF in 1987) reflected further endorsement of the idea that the adjustment process in low-income countries required an even longer time frame than implied by the EFF. However, the creation of concessional windows for the low-income countries also paved the way for a renewed emphasis on the temporary nature of the IMF's support in other countries. Thus, when the EAP was abandoned in 1992, its features related to the longer program and repayment periods were not retained in the new access policy, unlike those related to the magnitude of access to IMF resources. Subsequently, in 2000, a general review of IMF facilities led to the introduction of repurchase expectations, shorter than repurchase obligations, to signal the importance attached to the temporariness of the IMF's support, along with other incentives to encourage a faster repayment of outstanding credit by members in a position to do so.

Prolonged use of the IMF's concessional resources

4. When the SAF and ESAF were created, both were originally envisaged as one-off operations to support adjustment in low-income countries with protracted balance of payments problems, during a relatively short period and with limited resources.⁴

¹Details on the various policies referred to in this chapter are provided in Annex 2.

²Executive Board Decision No. 4377-(74/144). Arrangements under the EFF would be for a period not exceeding 3 years, to be lengthened to 4 where appropriate, with a repayment period of 4½ to 10 years.

³Executive Board Decision No. 6783, para. 3, 6, and 10. Purchases made under the EAP were to be repaid within 7 years. This decision stressed the temporary character of the EAP, hence the requirement of annual reviews of the policy. However, the EAP was not allowed to lapse until 1992.

⁴As under the EFF, resources were to be committed in support of a three-year program, with a repayment period of 4½ to 10 years.

These facilities were not only concessional but also had a less demanding adjustment requirement than the EFF: specifically, programs supported by these facilities were not required to solve the balance of payments problem fully, but only to assure substantial progress in that direction. The original decisions establishing the facilities precluded the possibility of entering into more than one three-year arrangement with any single country, largely because of the limited availability of resources to fund the facilities and the short time frame set for the commitment period. This restriction was not entirely consistent with the recognition that the programs might not solve the problem within the time frame. It was gradually abandoned in several steps taken between 1990 and 1997, as experience showed that the initial estimate of the time frame needed for effective adjustment in low-income countries had proved overoptimistic, and also as more financing became available. However, the Executive Board consistently stressed that the purpose of these successive extensions was *not to provide a source of continuous financing for individual countries*, but rather to maintain the IMF's ability to respond to members' needs as they arose.⁵

5. A further step was taken in 1999, with the transformation of the ESAF into the PRGF and the close relationship established between the latter and countries' Poverty Reduction Strategy Papers (PRSPs), which are meant to provide a longer-term framework for donor support to low-income countries. This framework does not presume an extended IMF involvement but—unlike the case earlier—it does not rule it out, thus generating some ambiguity.

6. In part, this evolution reflected the understanding that the countries concerned were particularly vulnerable to exogenous shocks and were in need of continued IMF support for their macroeconomic policies. However, another factor was the growing pressure from official creditors and donors for an IMF-supported program with IMF monitoring, as a “seal of approval” for debt relief and donor support (see Chapter 6).

Evolution of the Strategy Vis-à-Vis Prolonged Use

7. Each time prolonged UFR was discussed by the IMF Executive Board, Directors expressed concern not so much about prolonged use per se, but at the persistence of balance of payments imbalances in spite of protracted financial support from the IMF. This suggests that their primary concern was the inef-

⁵Cf. Chairman's summing-up of EBM/97/5, EBM/97/8, and EBM/97/10.

fectiveness of programs in achieving sustainable balance of payments adjustment. In each review, various remedial measures of increasing specificity were proposed by the IMF staff and endorsed by the Board. However, the Board consistently opposed imposing fixed limits on the length or extent of reliance on IMF support, out of concern that such limits might prevent the IMF from responding flexibly to members' needs as they arose. The Board also opposed endorsing any specific operational definition of prolonged use, owing to concerns that any definition would be arbitrary and assuming that good judgment would be sufficient to identify problematic cases of prolonged use. However, in practice, very few countries were even identified as prolonged users in staff reports to the Board,⁶ which may account in part for the lack of consistent implementation of the guidelines approved by the Executive Board.

Program design elements

8. All internal reviews of prolonged UFR identified inadequate program design and weak program implementation as key factors underlying prolonged use. The remedies envisaged focused on two aspects: the nature of conditionality and the extent of access.

Conditionality

9. From 1985 onward, successive staff reports endorsed by the Board proposed dealing with prolonged use through (i) greater emphasis on prior actions and frontloading of policy measures, especially those related to past policy failures; (ii) a proactive use of conditionality—in particular, the use of more detailed conditionality covering structural aspects; and (iii) on a case-by-case basis, a tranching of the IMF financial support such that disbursements would be backloaded. In addition, the 1991 review recommended building policy contingencies into programs, along with IMF contingency financing if appropriate.

10. In fact, actual practice with regard to prolonged users did not correspond to the remedies suggested in the reviews (see Chapter 5).⁷ Contrary to

⁶Based on a keyword search in the text of country reports recorded in the IMF's institutional repository, the only countries specifically characterized as prolonged, repeat, or long-term users in staff reports to the Board since 1983 are Argentina (2), Bulgaria (1), Cameroon (1), Côte d'Ivoire (1), Dominica (1), Jamaica (2), Malawi (1), Morocco (3), Pakistan (1), the Philippines (5), Senegal (1), and the Federal Socialist Republic of Yugoslavia (1). The figure in parentheses indicates the number of reports in which the terms above are mentioned.

⁷In assessing compliance with prolonged use guidelines throughout this chapter, for lack of a single officially recognized definition of countries to which these guidelines should be applied, we have used our own definition of prolonged use. Since it tends to be more demanding than the ones suggested by staff at

the policy directions endorsed by the Board, prolonged users as a group were actually subject to fewer prior actions and performance criteria, and even had slightly more frontloaded schedules of disbursement, on average, than “temporary” users.⁸ However, as discussed in Chapter 5, there is little evidence that the extent of conditionality per se— as opposed to ensuring that it is well prioritized and integrated into program design—was an important determinant of a program’s successful implementation. In that narrow sense, the nonimplementation of these aspects of the guidelines was probably not a major cause of prolonged use. However, that does not mean the design of conditionality is unimportant; we will return to this issue in Chapter 5.

Access to IMF resources

11. The general policy on access to IMF resources adopted in 1984 and still applicable today provided that “in determining the case for further Fund support and the amount of access in those cases where members have made repeated use of Fund resources, more careful attention will be given to the past record, the design of adjustment programs and the effectiveness of their implementation.”⁹ In 1991, this policy was reinforced by making explicit that its purpose was to seek a net reduction in prolonged users’ outstanding liabilities to the IMF, through a strengthening of programs and, possibly, a greater use of arrangements involving only limited access to IMF resources, but which could serve as a catalyst in mobilizing resources from other creditors.¹⁰ Later in the 1990s, as UFR policies became more differentiated between the GRA and the ESAF/PRGF Trusts, the

the time of various reviews, it seems fair to expect that most of the countries we define as prolonged users should have been subjected to these guidelines.

⁸It was not possible in the context of this study to assess on a large scale to what extent the recommendations related to contingency planning were followed, but evidence from the case studies suggests they were not. Furthermore, like the recommendations related to the use of conditionality, they do not appear to have ever been translated into actual operational guidelines for IMF staff.

⁹“Access Limits for 1985, Preliminary Policy Considerations” (EBS/84/168). To some extent, this is only an adaptation to the specific case of repeat users of the general guidelines on access adopted in 1983, according to which “*the amount of the member’s outstanding use of Fund credit and its record in using Fund resources in the past must enter into the judgment on the appropriate scale of further use of the Fund*” (EBS/83/233).

¹⁰“Selected Operational Issues Related with the Use of Fund Resources” (EBS/91/108). Similarly, in the 1990 Board discussion on “Strengthening the Cooperative Strategy,” Executive Directors had said that when there is evidence of repeated failure in program implementation, continued access to IMF resources would need stronger policy justification.

need to reduce access over time, even to concessional resources, was confirmed.

12. Our evaluation shows that these guidelines were not applied consistently in practice. In particular, our case studies show that the justification of the level of access proposed in staff reports was treated in a rather perfunctory manner. A broader look at the evolution of the level of access further indicates that only about one-fifth of prolonged users had a consistently diminishing access to either general or concessional resources.¹¹

Strengthened analytical and assessment efforts

13. The area of greatest consensus in dealing with prolonged users since the first time the Board reviewed the issue was the need to improve the understanding of the factors underlying a country’s prolonged need for IMF resources. This was to be achieved through a two-pronged analysis:

- a review of the historical background to a member’s problems and an analysis of the factors underlying its prolonged use experience at the time a new request for UFR was introduced;
- candid ex post assessments of performance under previous programs. The need for such assessments was repeated in successive Board discussions with increasing specificity over time.

However, the case studies show that these recommendations were generally not followed. A noteworthy exception is Morocco, whose entire IMF-supported adjustment experience was reviewed in 1994 as part of that year’s Article IV consultation. However, the practice was not followed for most prolonged users during the 1990s, although, as will be discussed later, somewhat more was done internally than was reported to the Board.

Exit strategies

14. As early as 1984, the IMF recognized that “frequently, despite the progress achieved during the period covered by an arrangement or a succession of arrangements with the Fund, *the amount of adjustment remaining to be accomplished at the end of the period was substantial.*”¹² Two remedies were envisaged to prevent such a situation from leading to pro-

¹¹The trend of access broadly reflects that of members’ gross financing needs, which also failed to decline consistently in a majority of cases. See Annex 2 for further evidence on the evolution of access.

¹²“Review of Upper Credit Tranche Arrangements and Some Conditionality Issues” (EBS/84/227).

longed UFR which, taken together, outlined an exit strategy from IMF lending.

Ex ante assessments of time needed to complete the adjustment process

15. In the early 1980s, it became a standard requirement for UFR staff reports to include a medium-term scenario, in order to identify *ex ante* cases where significant balance of payments gaps could be expected to persist over the foreseeable future. Subsequently, IMF staff was further requested to foresee a time frame for the disengagement of the Fund, particularly when prolonged users were involved.¹³ Evidence from the case studies again suggests that this recommendation was often not followed.

Strengthened surveillance at the post-program stage

16. Surveillance has long been identified as an important instrument for promoting the sustained implementation of adjustment efforts beyond the immediate UFR period.¹⁴ “Continued policy dialogue” was actually put on a par with improved program design to contain prolonged use. This was meant to involve anything between interim Article IV consultations and “shadow programs,” almost as detailed as UFR programs, but not linked to any IMF resources. This approach to safeguarding the IMF’s general resources beyond the program period received renewed emphasis in the 2000 “Review of IMF Facilities,” in the form of “post-program monitoring” (PPM). For concessional resources, the principle of post-program monitoring as a means of avoiding prolonged use was formally established in the early 1990s.¹⁵

17. However, few prolonged users have ceased to make use of IMF resources for longer than a simple interruption between programs and, among those

that did, few went through any of the envisaged exit strategies.¹⁶

Implications for other creditors

18. A key implication of the exit strategy outlined above was that, if the IMF was not prepared to provide financial support to its members for the entire period required to achieve a sustainable balance of payments situation, other donors and creditors would have to provide the necessary financing beyond the program period. This delicate problem was recognized in 1991, when a staff report noted that: “In cases where external viability is not in reasonable prospect, the Fund will need to carefully limit further provision of its resources. . . . Other creditors and sources of funds would then have to assume more of the responsibility for providing appropriate financing.”¹⁷ In the event, although the Executive Board endorsed the staff’s analysis, such a sequencing of IMF and donors’ financing has largely failed to materialize, in part as a result of creditors and donors continuing to insist on an IMF lending arrangement as a “seal of approval” (see Chapter 6).

19. In conclusion, the evolution of IMF policies responding to changing circumstances and perceptions have contributed to the phenomenon of prolonged use of its resources in several ways. First, the evolution of the IMF’s facilities intended to address more deep-seated causes of external problems, especially in low-income member countries, clearly increased the likelihood of prolonged use, though it did not fully and explicitly recognize the potential consequences. This appears to have reflected in part differences of view within the Executive Board over what the longer-term role of the IMF should be in such cases.¹⁸ As a result, the IMF has been left with a mismatch between its core operational approach (which is still focused on promising and achieving a restoration of sustainability within a relatively short time frame) and some of the tasks it is being asked to perform. As will be seen in subsequent chapters, this

¹³“Selected Operational Issues Related with the Use of Fund Resources” (EBS/91/108) recommended “systematically highlighting, in staff reports accompanying requests for UFR arrangements by prolonged users, the prospects for continued need for Fund resources in the future and, where possible, indicate the time frame and circumstances in which UFR might no longer be needed.”

¹⁴See “Review of Upper Credit Tranche Arrangements and Some Conditionality Issues” (EBS/84/227) and “Issues in the Implementation of Conditionality: Improving Program Design and Dealing with Prolonged Use” (EBS/85/265).

¹⁵“Operational Modalities and Funding Alternatives for an ESAF Successor—Preliminary Considerations” (EBS/93/32). Subsequently, it was also envisaged that one option for continued IMF support for the programs of former ESAF users that ceased to have a need for IMF financing would be through precautionary arrangements, but that option was eventually not pursued.

¹⁶Among prolonged users, The Gambia and Bangladesh went through the “enhanced surveillance” procedure in 1993/94, as did Uruguay and the Federal Socialist Republic of Yugoslavia in the late 1980s. Ecuador had a staff-monitored program in 1995/96, and the Philippines entered the post-program monitoring procedure after its last arrangement expired in 2000. In all these cases, these procedures were applied to the country after a long string of IMF-supported programs. Of these countries, Bangladesh and the Philippines are the only two which, to date, have not made further UFR.

¹⁷“Selected Operational Issues Related with the Use of Fund Resources” (EBS/91/108).

¹⁸The discussion in Annex 2 of the evolution of policies on the use of concessional resources provides further illustration of this point.

question of time frame lies at the heart of many of the problems associated with prolonged use.

20. Second, although the Board did on various occasions approve the elements of a strategy to reduce prolonged use, this has not been systematically implemented. A contributory factor here is the absence of formal definition of prolonged use, although various proposals have been made by IMF staff. In the absence of a formal definition, there is ambiguity about whether procedures prescribed to deal with prolonged use need to be followed in particular cases.

21. Finally, questions of financing have strongly influenced the approach to prolonged use. Initially, the limited availability of funding for the IMF's con-

cessional facilities precluded any consideration of a long-term involvement. Subsequently, the fact that the level of aid flows was not always consistent with the intended diminished reliance of SAF/ESAF users on IMF lending implied that the IMF would have to either remain involved until a sustainable external situation could be reached, no matter how long it took; or leave the countries concerned midway in this process, with a high probability of backsliding. Both options involved some departure from the IMF's original mandate, and the choice taken—to remain involved—while perhaps the only practical one under the circumstances, only deepened the mismatch with the IMF's operational approach mentioned above.