July 2018

Office of the Nordic-Baltic Constituency

VIEWS AND POSITIONS ON POLICY DEVELOPMENTS IN THE INTERNATIONAL MONETARY FUND

Semi-Annual Report

Contents

1 INTRODUCTION

This report provides an overview and status of the main Executive Board discussions and other IMF related issues during the first half of 2018, and outlines the view of the Nordic-Baltic constituency (NBC) on these issues. The first section of the report summarizes the global economic and financial developments, which provides the backdrop for the work program of the Executive Board over the next twelve months. The remaining part of the report is structured around the three pillars of the Fund's work: surveillance, lending, and capacity development. First, the Executive Board's work on surveillance and economic policy is presented, including the bilateral and regional surveillance activities of the first half of 2018, as well as some of the major economic policy items on the Board's agenda during the reporting period. The second section on lending provides an overview of the new Fund-supported programs and reviews conducted by the Executive Board during this period. The third section gives a brief status on the Executive Board's involvement in the upcoming review of the Fund's capacity development strategy. Finally, the fourth section reports on the activities of the IMF's Independent Evaluation Office.

1.1 Global Economic & Financial Developments

CONTEXT: The global economic backdrop for the workings of the Fund and of its Executive Board during the first half of 2018 was of a strengthened global economic upswing. On April 2, 2018, the Executive Board discussed the flagship reports of the Fund: The World Economic Outlook (WEO), the Global Financial Stability Report (GFSR), and the Fiscal Monitor. The April WEO emphasized that the economic upswing had become broader, driven by an investment recovery and strong trade growth, supported by accommodative monetary policy in most countries and favorable global financing conditions. In the short-term, this recovery was expected to continue, with the additional stimulus of a substantial fiscal expansion in the US. For many countries, the current favorable growth rates are not expected to last as growth rates will eventually bend towards their weaker longer-term levels. Particularly, advanced economies are growing faster than their growth potential, which could lead to bottle-necks down the road. These short-term expansionary dynamics also set the stage for the medium-term risks, which is compounded by low productivity growth and aging populations in the advanced economies.

The Global Financial Stability Report found that short-term risks to financial stability had increased somewhat over the last six months. It also highlighted the still elevated medium-term financial vulnerabilities, which have built up during the years of accommodative policies, could mean a bumpy road ahead and put growth at risk. Higher inflation may lead central banks to respond more aggressively than currently expected, which could lead to a sharp tightening of financial conditions. Valuations of risky assets are still stretched, and liquidity mismatches, leverage, and other factors could amplify asset price moves and their impact on the financial system. The GFSR additionally underlined the vulnerability of Emerging Markets to the tightening of global financial conditions.

Since then, the Fund has presented its updated assessment in the July World Economic Outlook Update. The global expansion has become less even, and appears to have peaked in some major jurisdictions. Some of the key risks to global growth, that had been identified earlier in the year, such as trade tensions, tightening of global financial conditions, and rising oil prices, have become more prominent and some have materialized. Moreover, the balance of risks has shifted further to the downside, also in the short-term. This essentially means that the global economy is experiencing some of the "bumps on the road" identified in the April flagship reports. Policies and reforms should aim at sustaining activity, raising medium-term growth, and enhancing inclusiveness. With the reduced economic slack and downside risks mounting, many countries need to rebuild fiscal buffers to create policy space for the next downturn and strengthen financial resilience to an environment of possibly higher market volatility. Policymakers and investors must remain attuned to the risks of rising interest rates and higher market volatility. Central banks should continue to normalize policy gradually and communicate clearly, and policymakers should address vulnerabilities by deploying and developing macroprudential tools.

NBC VIEW: The NBC agreed with the Fund's assessment in the April flagship reports, and the updated July World Economic Outlook. The NBC emphasized the need to use the current upswing to build buffers and enhance resilience, and avoid pro-cyclical policies. The NBC also strongly supports multilateralism, open and rules-based international trade, and that all policy makers should refrain from engaging in protectionism and inward-looking policies.

FURTHER READING: April 2018 World Economic Outlook April 2018 Global Financial Stability Report April 2018 Fiscal Monitor July 2018 World Economic Outlook Update

1.2 The Work Program of the Executive Board

CONTEXT: In June, the Executive Board discussed the Managing Director's Statement on the Work Program of the Executive Board. The Work Program translates the strategic directions and policy priorities laid out in the Spring 2018 Global Policy Agenda and the International Monetary and Financial Committee Communiqué into an Executive Board agenda for the next twelve months. Within the three pillars of the Fund, surveillance, lending, and capacity development, the main policy priorities and deliveries were in broad categories: (i) Enhance resilience, rebuild policy space, and implement reforms to sustain the upswing, through the Fund's regular multilateral and bilateral surveillance products. (ii) Collaborate within a multilateral system and address shared challenges, with emphasis on the benefits of an open and rules-based multilateral trade system, continue work on experiences with capital flow management measures and the implementation of the Fund's institutional view, and outline opportunities and risks of financial digitalization, and a more comprehensive work program on the impact of digitalization more broadly, as well as more analytically assess international taxation issues. (iii) Upgrade tools to develop tailored policy solutions, with emphasis on developing a multi-pronged approach to help address debt distress problems in some low-income countries (LICs) and improve debt management capacity and transparency, and (iv) Improve the governance of the Fund with a view to completing the 15th general Review of Quota by the 2019 Spring Meetings, and no later than the 2019 Annual Meetings. The Work Program also contains items intended to further develop the Fund's ability to engage on emerging issues such as inclusive growth, gender inequality, and governance and corruption issues.

NBC VIEW: The NBC supported the policy priorities laid out in the Managing Director's statement on the Work Program. The NBC places strong emphasis on the Fund continuing to promote an open and rules-based trading system in line with its founding mandate. The NBC also strongly agreed that building policy buffers and strengthening resilience is among the top policy priorities in the current environment, as well as reiterated its support for the Fund to analyze and engage on emerging issues such as digitalization, Fintech, inclusive growth, gender and income inequality, as well as governance and corruption.

FURTHER READING: Statement by the Managing Director on the Work Program of the Executive Board - Executive Board Meeting - June 18, 2018

2 SURVEILLANCE & ECONOMIC POLICY

A core part of the Fund's implementation of its mandate is to conduct economic and financial surveillance. To enable the Fund to conduct bilateral surveillance, each member of the Fund is required to provide it with the necessary information and to consult with it when requested. During the first half of 2018, the Executive Board concluded Article IV consultations with 65 countries across all regions. For three of these countries, the Article IV report was accompanied by a comprehensive Financial System Stability Assessment, which is a more resource intensive exercise conducted less frequently than Article IV consultations. In addition, the Board was briefed by the various area departments of the Fund on regional developments, and the Board discussed several economic policy issues prepared by Fund staff.

2.1 Bilateral & Regional Surveillance

2.1.1 Macroeconomic Developments in Low-Income and Developing Countries

CONTEXT: In March, the Executive Board discussed Macroeconomic Developments and Prospects in Low-Income Developing Countries, and assessed economic prospects and policy challenges facing the low-income developing countries (LIDCs) against the background of a climbing number of LIDCs at high risk or in debt distress.

Growth prospects for LIDCs are improving, supported by improved external conditions. However, this more favorable outlook is subject to a range of risks, including from a reversal of the recovery in commodity prices, an unexpectedly sharp tightening of global financial conditions, domestic policy slippage, internal conflict, weather shocks, and rising financial sector stress.

There has been a broad-based weakening of fiscal positions in LIDCs in recent years, with fiscal deficits widening in some 70 percent of LIDCs between 2010-14 and 2017. In about one-third of these cases, higher public borrowing was fully matched by a scaling-up of investment, but in close to half the cases investment declined, notwithstanding higher public borrowing.

Debt burdens and vulnerabilities have risen significantly since 2013 in many LIDCs, reflecting a mix of factors including exogenous shocks and loose fiscal policies. While the majority of LIDCs remain at low or moderate risk of debt distress, the number of countries at high risk or in debt distress has increased from 13 in 2013 to 24 (over 40 percent of LIDCs) in January 2018.

The composition of public debt in LIDCs continues to shift from traditional sources towards non-Paris Club bilateral lenders, commercial external debt, and domestic debt. Higher interest rates on commercially-priced debt has led to higher debt servicing costs and market risks, while the rising importance of non-traditional creditors poses new challenges for potential debt resolutions.

Data on LIDC debt suffer from substantial gaps, notably related to public guarantees and to debt of public sector entities outside the general government. This can result in significant underestimation of public sector liabilities, while undermining the value of debt sustainability analyses. Data gaps have contributed to unfavorable debt surprises in several countries, as public liabilities not captured in the debt data are converted into liabilities of the central government.

NBC VIEW: The NBC encouraged the IMF and the World Bank to further intensify their collaboration in in LIDCs, including to help promote quality investment of scarce resources in projects with large economic and social returns. Considering the increasing debt levels, the NBC emphasized that risks to debt sustainability need to be managed carefully to avoid another large-scale sovereign debt crisis in low-income countries.

Concerted efforts from the multilateral community and country authorities to build capacity, strengthen debt sustainability analysis, and improve data coverage are needed to bring debt levels to sustainable levels. The NBC stressed that the IMF together with the Paris Club, and other creditors, need to continue working together to enhance the cooperation on debt issues. All lenders and borrowers should adhere to global principles for sustainable lending and borrowing.

FURTHER READING: Macroeconomic Developments and Prospects in LIDCs

Box 1. Selected IMF Article IV consultations under the first half of 2018

Denmark: The Executive Board concluded the 2018 Article IV consultation for Denmark in June. The Article IV report found that Denmark continued to enjoy solid economic growth. Unemployment is low and there are signs of labor shortages and capacity constraints in some sectors, which in turn constrains Denmark's growth potential. The report therefore explored various ways to increase the labor supply further and increase growth potential through, e.g. incentivizing private investment. The report found that the financial system is sound with well-capitalized banks, but that house price pressures in some urban areas combined with elevated household debt creates risks that should be mitigated through tightening of existing macroprudential measures and structural measures that can ease restrictions on the supply of housing. The report also found that the external position was assessed to be stronger than fundamentals, but that structural policies that raise investment would help balance the external surplus. The Danish authorities broadly agreed with staff's assessment and endorsed staff's appraisal. For more information, read the full report here.

Estonia: In May, the Executive Board concluded the Article IV consultation for Estonia, endorsing the staff appraisal without a Board meeting. After several years of subdued growth, Estonia's real GDP grew by 4.9 percent in 2017, more than double the rate achieved a year earlier. The report found Estonia's economic fundamentals strong and financial soundness indicators solid. The output gap has turned positive, labor force participation is historically high, and confidence indicators rose throughout 2017. Inflation is running above the EU average and the current account is in surplus. However, income convergence has slowed and adverse demographics persist. Public finances were assessed as healthy, with a small overall fiscal deficit and low debt. In the context of a continued positive output gap, rising inflation pressures and a tightening labor market, report's advice focused on a broadly neutral fiscal policy that protects productivity-enhancing investments. With Estonia's potential growth constrained and strains on competitiveness emerging, policies to boost productivity, labor supply and innovation should be accelerated while wage growth needs to be gradual and anchored by fundamentals. For more information, read the full report here.

Lithuania: The Executive Board concluded the Article IV consultation with the Republic of Lithuania in June. The Article IV report found that Lithuania's economic performance has been impressive, but that the country now risks falling into the middle-income trap. External and internal imbalances have been corrected, but significant medium-term challenges have yet to be addressed. These include tackling adverse demographics, transitioning from a low-wage to high-productivity growth model and addressing high income inequality. Addressing these challenges would require ambitious structural reforms. The Lithuanian authorities broadly agreed with the thrust of the staff appraisal. For more information, read the full report here.

Euro Area: In July, the Executive Board concluded the Article IV consultation on Euro Area Policies as well as the accompanying Financial System Stability Assessment. The reports found that the euro area expansion, while still vigorous, is slowing to a more moderate pace. The main engine remains domestic demand, underpinned by solid job creation. An array of global and domestic risks hangs over the outlook. Trade tensions have risen and further escalation looms as a major risk. Meanwhile, policy inaction and political shocks at the national level are the biggest domestic risks, especially the lack of sufficient effort in countries with high public debt to rebuild fiscal buffers and implement structural reforms. On the financial sector, there has been significant progress on the banking union. The size and quality of banks' buffers are higher than before, and nonperforming loans have declined, but low profitability remains a chronic problem for many banks. Banking supervision has undergone a steep improvement with the creation of the Single Supervisory Mechanism, and the handling of bank resolution under the Single Resolution Mechanism, although the fragmentation of rules along national lines remain an issue. The reports lay out detailed recommendations for further improvement. The NBC was in broad agreement with most of the findings and recommendations in the Article IV staff report and Financial System Stability Assessment. For more information, read the full Article IV report here and Financial System Stability Assessment here.

U.S.: The Executive Board concluded the Article IV consultation with the United States in late June. The Article IV report found that the near-term outlook for the US economy is one of strong growth and job creation. Growth is set to accelerate, aided by a fiscal stimulus, a recovery of private investment, and supportive financial conditions, as well as a favorable external environment. Despite good near-term prospects, several vulnerabilities are building up. The planned expansion in the federal deficit at this stage of the cycle could trigger a faster-than-expected rise in inflation. That would be accompanied by a more rapid rise in interest rates that could increase market volatility both in the US and abroad. The net effect of the US budget and tax policy choices will exacerbate an already unsustainable upward dynamic in the public debt and leave few budget resources available to invest in a range of urgently needed supply-side reforms, including infrastructure spending. It will also contribute to a rise in global imbalances. These risks are added to by recent actions by the US to impose tariffs on imports. The NBC agreed with the thrust of the staff appraisal. For more information, read the full report here.

China: In July, the Executive Board concluded the Article IV consultation with China. The report sees China at an historic juncture as the authorities are shifting their policy focus from demand side stimulus and high-speed growth to supply-side structural reforms and high-quality growth. The economy continues to perform strongly and reforms have progressed in several key areas, financial sector de-risking has accelerated, overcapacity reduction and opening-up of the economy have proceeded. Rebalancing continues, with growth becoming less dependent on credit and current account surplus continuing to fall, but its progress has slowed, with exports rather than consumption driving the growth pick up. The credit expansion has moderated somewhat but remains excessive, with staff advising the authorities to stay the course on tightening macro-financial settings. Strong domestic momentum and significant reform process underpin the near-term positive growth outlook. Risks, however, are tilted to the downside, particularly the rising external risks with the recent escalation of trade tensions. While the initial direct effects of tariff measures on Chinese exports announced by the US seem limited, escalating tariffs and investment restrictions could disrupt supply chains and weaken confidence and investment in China. For more information, read the full report here.

2.2 2018 External Sector Report and Revised Methodology

CONTEXT: On July 16, the Executive Board discussed the 2018 External Sector Report (ESR). The IMF's 2018 ESR shows that global current account balances stand at about 3¼ percent of global GDP. Of this, 40-50 percent are now deemed excessive, i.e. some countries are saving too much, and others are borrowing too much. This finding matters because persistent excess imbalances may become unsustainable, putting the global economy at risk and aggravating trade tensions. They can also make deficit countries vulnerable to sudden reversals of capital flows, when lenders get nervous and pull out their money. The report also found that protectionist policies should be avoided as they are likely to have significant deleterious effects on domestic and global growth, while limited impact on external imbalances. Surplus and deficit countries alike should work toward reviving liberalization efforts and strengthening the multilateral trading system.

The 2018 ESR applied a refined methodology aimed at providing a stronger, conceptually grounded modelling of the main drivers of current account balances, incorporating advances in the literature and extensive feedback from country authorities. Refinements focused on improving the modeling of certain features such as demographics, the measurement of external positions, and institutional quality, macroeconomic policies such as foreign exchange intervention and credit excesses, in the EBA current account model. Complementary tools were also developed to evaluate the role structural policies could play in reducing imbalances.

NBC VIEW: The NBC broadly agreed with the assessment and key takeaways in the report, including policy recommendations, and that global imbalances should be addressed in a growth-friendly manner with decisive and comprehensive policy action – stimulating investment and consumption in excessive surplus countries, and policies to boost productivity and competitiveness in excess deficit countries. Procyclical policies should generally be avoided. The NBC viewed the refined methodology as an improvement, but that further refinements to better account for the design of pension systems and merchanting trade should be explored. The NBC emphasized that the EBA methodology should be used as input to the Fund's overall external balance assessment, and that staff judgement remains essential to assess the model outcome.

FURTHER READING: 2018 External Sector Report: Tackling Global Imbalances amid Rising Trade Tensions

2.3 Assessing Fiscal Space

CONTEXT: In May, the Executive Board discussed the IMF policy paper on Assessing Fiscal Space: An Update and Stocktaking. The paper reviews the experience with the fiscal space assessment framework that was piloted in Fund surveillance during 2017–18. Fiscal space is defined as the room for undertaking discretionary fiscal policy relative to existing plans without endangering market access and debt sustainability. The framework is multi-dimensional, with IMF staff judgment and country-specific factors playing a significant role in the final judgment. It was developed in response to the need to provide a more systematic approach to assessing fiscal space in the context of Fund surveillance. It serves as a tool to inform assessments of the availability of fiscal space over a three to four-year horizon. The framework generally worked well across the various pilot countries, generating assessments that were broadly in line with its underlying logic and indicators. The implementation of the framework also revealed a few potential areas for modification to further support fiscal space assessments in country-specific contexts, such as exposure to shocks, economic structure and level of development. Such extensions include a more formal integration of contingent liabilities, as well as adjustments to capture the specificities of commodity producers and low-income countries who obtain a significant amount of external market or other non-concessional financing.

NBC VIEW: The NBC welcomed that the framework has provided a structured approach for assessing fiscal space in a way that is comparable across countries. The NBC appreciate that the framework's design had been made sufficiently flexible to take into account relevant conditions in individual countries. This is particularly important since fiscal space is a multi-dimensional concept and difficult to pin down purely through a mechanical rule or threshold. It was also welcome that the framework explicitly requires that the question of the existence of fiscal space is separated from its use. The NBC supported the proposal to expand the use of the framework as a regular tool in Fund surveillance.

FURTHER READING: Assessing Fiscal Space: An Update and Stocktaking

2.4 Program Design in Currency Unions

CONTEXT: In February, the Executive Board discussed general guidance on the design of Fund-supported programs with members of currency unions. The guidance more specifically addresses Fund engagement with currency union-level institutions, where currency union members have delegated important economic and financial policies to union-level institutions, and in circumstances where the policies of these institutions are critical to the success of Fund-supported programs in individual members of the currency union. The general guidance includes policy assurances from union-level institutions, its form, and the need for assurances to be clear, specific, monitorable and—where necessary—timebound.

NBC VIEW: The NBC supported the general guidance on the design of Fund-supported programs with members of a currency union. The NBC stressed, in line with the consensus of the Executive Board, that that the legal, institutional, and policy frameworks differ across currency unions, and that such differences need to be considered, on a case-by-case basis, and that the Fund will not seek policy assurances from a union-level institution that would involve it taking actions that are inconsistent with that institution's mandate and legal and institutional frameworks.

FURTHER READING: IMF Executive Board Discusses Program Design in Currency Unions
Program Design in Currency Unions

2.5 2018 Interim Surveillance Review

CONTEXT: As part of the IMF's continuous reviews of its surveillance function, the Executive Board in April discussed the 2018 Interim Surveillance Review. This interim review focused on progress in implementation of areas identified in previous reviews. Fund surveillance has become better adapted to the global conjuncture, and more integrated and risk-based. There has also been progress in core areas such as risk work, fiscal and external sector analysis, and in integration of macro-financial analysis and of macro-structural policy work that aims to reinvigorate productivity and growth. The Interim Surveillance Review also considered actions to be taken to further enhance surveillance ahead of the Comprehensive Surveillance Review in 2019. Examples of such actions include refinements to external sector assessments, sustaining progress on macro-financial surveillance, addressing data gaps, and incorporating lessons from pilot efforts including on macro-financial, macro-structural and emerging issues. In future work, the Fund will build on lessons learned from implementing previous surveillance reforms. The 2019 Comprehensive Surveillance Review will further anchor the Fund's surveillance in a world of rapid technological change.

NBC VIEW: The NBC commended the IMF for being agile to the membership's needs and making substantial improvements to the surveillance toolkit in recent years. The enhanced focus on financial surveillance and macro-financial linkages was strongly endorsed by the NBC. When risks migrate into new areas, it is important that the IMF is vigilant. The NBC also stressed further emphasis on risk analysis, spillovers, and spillbacks and that it is duly incorporated into the Fund's bilateral surveillance. To improve traction, it was suggested that follow-up to previous Fund policy advice should be more notable in Article IV and FSAP reports. Going forward, the NBC stressed the need to make sure the 2019 Comprehensive Surveillance Review covers areas that have gained importance since the last comprehensive review.

FURTHER READING: The 2018 Interim Surveillance Review

2.6 Review of the 1997 Guidance Note on Governance

CONTEXT: In April, the Executive Board adopted the policy framework outlined in a staff paper on "Review of 1997 Guidance Note on Governance—A Proposed Framework for Enhanced Fund Engagement." The new framework supplements the existing policy on governance. The paper outlines the principles that will continue to underpin the Fund's engagement on governance issues in surveillance and use of Fund resources, and provides a Framework for Enhanced Fund Engagement. The Framework is designed to promote more systematic, effective, candid, and evenhanded engagement with member countries regarding governance vulnerabilities, including corruption, that are judged to be macroeconomically critical. The Framework consists of four elements:

The first element is designed to enable the Fund to assess the nature and severity of governance vulnerabilities—including corruption. This includes an assessment of those state functions that are most relevant to economic activity, namely (i) fiscal governance; (ii) financial sector oversight; (iii) central bank governance and operations; (iv) market regulation; (v) rule of law; and (vi) Anti-Money Laundering and Combatting the Financing of Terrorism.

The second element will guide the Fund's assessment of the macroeconomic implications of governance vulnerabilities taking into account the applicable standards for surveillance and the use of Fund resources. The paper lays out empirical evidence of the negative impact of governance vulnerabilities on economic performance, which provides a strong basis to determine that these vulnerabilities should be addressed in surveillance when they are assessed as severe.

The third element provides a framework for policy advice and capacity development support to members where Fund engagement is warranted, while the fourth element focuses on measures designed to prevent the private actors from offering bribes or providing services that facilitate concealment of corruption proceeds.

NBC VIEW: The NBC has been a long-standing promoter of transparency and good governance and reiterate its support for the Fund's work in this context. Overall, the NBC agreed with the conclusion that the general approach of the 1997 Guidance Note remained appropriate when addressing governance weaknesses, including relevant policies adopted since the note was first approved, notably the Guidelines on Conditionality from 2002 and the Integrated Surveillance Decision from 2012. At the same time, the previous review identified several areas where the Fund's engagement should be strengthened. To address these shortcomings, the NBC supported staff's proposal to adopt a framework which would supplement the 1997 Guidance Note.

FURTHER READING: Review of 1997 Guidance Note on Governance - A Proposed Framework for Enhanced Fund Engagement

3 LENDING

3.1 Standard Lending Facilities

During the first half of 2018, the Executive Board has approved one new loan under the standard non-concessional lending facilities, which was for Argentina, c.f. below. Among the ongoing lending arrangements, the Executive Board completed reviews of Fund-supported programs for Bosnia & Herzegovina, Tunisia, Mongolia, Jamaica, Sri Lanka, Cote d'Ivoire, Georgia, Moldova, and the Arab Republic of Egypt. Meanwhile, Post-Program Monitoring was completed for Portugal, Pakistan, Albania and Cyprus. The NBC supported the new loan under the Stand-by Arrangement for Argentina, as well as the reviews completed during the first half of 2018. Some of the major Fund-supported programs are described in more detail below.

3.1.1 Argentina

CONTEXT: On June 20, 2018, the Executive Board approved a three-year Stand-By Arrangement (SBA) for Argentina amounting to USD 50 billion. Argentina's financial markets came under sudden pressure in April as the result of a confluence of factors. A severe drought led to a sharp decline in agricultural production and export revenue, world energy prices increased, and global financial conditions tightened through an appreciation of the U.S. dollar and an upward shift in U.S. interest rates. These changes interacted with vulnerabilities that Argentina's policy path had embedded, including significant fiscal and external financing requirements. The Board's decision allows the Argentinian authorities to make an immediate purchase of USD 15 billion, and the remaining amount of IMF financial support (USD 35 billion), which the authorities indicated they intend to treat as precautionary, will be made available over the duration of the arrangement, subject to quarterly reviews by the Executive Board. The Fund-supported program and the associated conditionality builds to a large extent on the plans of the authorities, and includes three major objectives: Restore market confidence and put public debt on a downward trajectory, protect society's most vulnerable, strengthen the credibility of the central bank's inflation targeting framework, and progressively lessen the strains on the balance of payments. The program is subject to quarterly reviews.

NBC VIEW: The NBC supported the lending facility under the Stand-By Arrangement, but underscored the risks associated with the large size of the program, and the substantial front-loading of access. The NBC encouraged clear ownership and steadfast program implementation by the authorities to ensure a successful completion of the program, to mitigate the social impact of the program, and to safeguard the financial resources of the Fund.

FURTHER READING: IMF Executive Board Approves US$50 Billion Stand-By Arrangement for Argentina   Argentina: Request for Stand-By Arrangement-Press Release and Staff Report

3.1.2 Egypt

CONTEXT: On June 29, the Executive Board completed the third review under the Extended Fund Facility with the Arab Republic of Egypt. The Board's decision allowed for the next tranche of USD 2 billion to be disbursed. The Executive Board commended the authorities for their strong program performance, and welcomed the authorities continued commitment to fiscal consolidation and structural reform. Given that the reforms have a short-term negative social impact, social spending, protecting the society's most vulnerable, is safeguarded under the program. The Egyptian authorities have taken strong ownership of the program. Given that the authorities are on track to achieve the planned three-year fiscal consolidation plan, banks remain financially healthy and resilient, and the initial program objectives have been fulfilled, the program is now shifting towards a broadening of structural reforms to support inclusive growth, job creation, and improved governance. The program is subject to semi-annual reviews.

NBC VIEW: The NBC supported the completion of the third review, also commending the authorities for their good program performance. The NBC emphasized that, while undergoing economic adjustment, to maintain public support of the program, social spending to protect society's most vulnerable need to be safeguarded. The NBC also underscored the need to reduce the role of the state in the economy to support private sector development.

FURTHER READING: Egypt: IMF Executive Board Completes Third Review under the Extended Fund Facility (EFF) Press Release; Staff Report; and Statement by the Executive Director for the Arab Republic of Egypt

3.1.3 Mongolia

CONTEXT: On June 27, 2018, the Executive Board completed the fourth review of the Extended Fund Facility for Mongolia. The Executive Board's decision allowed for the next tranche of USD 36.9 million, to be disbursed. The Fund-supported program, and the financial support from the Fund, acts as an anchor for a larger financing package including a multitude of contributors. The program performance under the program continues to be strong. There is overperformance on key fiscal and international reserve targets, while structural reforms to strengthen fiscal policy and the banking sector is moving ahead. Debt remains elevated and the economy continue to be exposed to global commodity developments, and continued program implementation is critical to mitigate this vulnerability. Social spending, protecting society's most vulnerable is protected under the program. Having achieved the needed macro-stabilization during the initial stages of the program, the focus is now shifting to a broader set of structural reforms, to ensure the long-term success of the program. The program is subject to semi-annual reviews.

NBC VIEW: The NBC supported the completion of the fourth review and emphasized the need continue steadfast program implementation, while safeguarding social protection. The NBC also underscored the need to reduce the sensitivity of the economy to individual mining projects, to prevent the boom-bust cycles of the past going forward, and focus on structural reforms that support the business environment and economic diversification.

FURTHER READING: IMF Executive Board Completes Fourth Review under the Extended Arrangement for Mongolia and Approves US$ 36.91 Million Disbursement Fourth Review under the Extended Fund Facility Arrangement and Request for Modification of Performance Criteria

3.1.4 Greece

CONTEXT: On June 21, 2018, the IMF Managing Director commended Greece and its European partners on the completion of the fourth and final review under the European Stability Mechanism (ESM) program. The additional debt relief measures will mitigate Greece's medium-term refinancing risks and improve its medium-term debt prospects, both of which are very welcome results. The Managing Director noted that while time has run out to enter into the Fund's Stand-By Arrangement, the Fund will remain fully engaged in supporting Greece in sustaining its economic recovery and achieving more robust growth in the post-program period, including post-program monitoring. On June 29, Fund staff issued a Concluding Statement of the 2018 Article IV mission.

FURTHER READING: Statement by the Managing Director on Greece Staff Concluding Statement of the 2018 Article IV Mission

3.1.5 Ukraine

CONTEXT: The fourth Review under the Extended Fund Facility for Ukraine is still pending. On June 19, 2018, the Managing Director stated that she was encouraged by the adoption of the law on the High Anti-Corruption Court by the Ukrainian parliament, which is an important step forward in the authorities' fight against corruption. The new law paves the way for setting up an independent and strong anti-corruption court that together with existing institutions (NABU and the Special Anticorruption Prosecutor's Office) will contribute to delivering the accountability and justice that the people of Ukraine demand of their public officials. The Managing Director welcomed the intention of President Poroshenko to make the court operational by the end of 2018. Further, the Managing Director underlined that it is important to work toward the timely implementation of this and other actions, notably related to gas prices and the budget, that are critical to allow the completion of the pending review under Ukraine's IMF-supported program. While the Review is pending, the Executive Board is briefed on developments on an ad hoc basis.

FURTHER READING: Statement by the Managing Director on Ukraine

3.2 Precautionary Lending Facilities

3.2.1 Colombia

CONTEXT: Colombia, who has had a Flexible Credit Line (FCL) arrangement with the IMF since 2009, was approved a new 2-year FCL arrangement of SDR 7.848 billion (about USD 11.4 billion) in May. The Colombian authorities consider external risks to be high and that an FCL arrangement provides a useful insurance in case risks materialize. The credit line is to be treated as precautionary. IMF staff's assessment is that the previous FCL arrangements have helped Colombia cope with heightened external risks and provided space to strengthen policies; and staff consider Colombia to have a good track record of strong policy implementation.

NBC VIEW: The NBC agreed that Colombia met the qualification criteria for an FCL and the request for a new arrangement. The FCL has been a good anchor and support for Colombia while dealing with large external shocks, and the authorities' strong economic fundamentals and appropriate policy responses have laid the foundation for the economic recovery. However, the NBC also underscored that prolonged use of the FCL should be avoided, given the intended temporary nature of the arrangement, and emphasized that the authorities should be ready to present a well-designed exit strategy when warranted, also a signal of strength to the markets.

FURTHER READING: Colombia: Arrangement Under the Flexible Credit Line and Cancellation of Current Arrangement

3.2.2 Morocco

CONTEXT: In January, the Executive Board completed the third review of Morocco's Precautionary Liquidity Line (PLL) arrangement. This two-year PLL arrangement of SDR 2.504 billion (about USD 3.61 billion) was approved by the IMF Board in July 2016 and expires in July 2018. The Moroccan authorities did not draw on the arrangement but treated it as precautionary. The aim of the program has been to support Morocco in rebuilding fiscal and external buffers and promoting higher and more inclusive growth.

NBC VIEW: Since Morocco continued to meet the qualification criteria and had continued to implement sound policies, albeit with some delay, the NBC supported the completion of the third review. The NBC stressed the need for continued fiscal consolidation to lower public debt and secure space for priority social spending, and accelerating the necessary structural reforms to promote higher and more inclusive growth. Risks associated with the high level of non-performing loans also need careful monitoring. The NBC highlighted the need for an exit strategy when conditions allow, underscoring the intended temporary nature of precautionary facilities.

FURTHER READING: Morocco: Third Review Under the Arrangement Under the Precautionary and Liquidity Line (PLL)

3.3 LIC Facilities

During the first half of 2018, the Executive Board has approved new Fund-supported programs with financial resources under the concessional lending facilities for Burkina Faso and Malawi, while it completed reviews of existing Fund-supported programs for Chad, Ghana, Islamic Republic of Afghanistan, Islamic Republic of Mauritania, Mali, Niger, Guinea-Bissau, Rwanda, Seychelles, Togo, Cote d'Ivoire, Benin, Guinea, and the Republic of Moldova. Some of the main policy items related to the Fund's lending to low income countries are outlined below.

3.3.1 LIC Facilities Review

CONTEXT: On July 20, the Executive Board discussed a staff evaluation of the Fund's facilities for low-income countries (LICs). The current toolkit of Fund facilities for LICs, introduced in 2009, comprises the Extended Credit Facility (ECF), aimed at helping countries tackle protracted balance of payments problems; the Standby Credit Facility (SCF), aimed at helping countries tackle short-term balance of payments problems or to put in place precautionary financing to respond to unexpected shocks; the Rapid Credit Facility (RCF), which provides emergency finance to countries hit by adverse exogenous shocks and financing to countries not yet in a position to enter into a Fund-supported arrangement; the Policy Support Instrument (PSI), which provides countries with a means of signaling strong economic policies and a platform for Technical Assistance. Financial support under these facilities is provided on concessional terms.

The review examined whether the basic structure of LIC facilities remains broadly appropriate to meet members' evolving needs; looked at the case for increasing access limits and modifying financing terms; and evaluated the case for specific adjustments to the facilities to ensure they appropriately address the financing needs of LICs. Based on the assessment by the Executive Board, staff will prepare specific proposals for Board discussion and approval in early-2019.

NBC VIEW: The NBC broadly agreed with the main conclusions of the paper's stock-taking. The NBC encouraged stricter scrutiny of debt dynamics in program reports, strengthen debt related data provision requirements for countries receiving IMF financing or technical assistance, and to facilitate close collaboration with non-Paris Club creditors on debt dynamics. The NBC believed that a comprehensive assessment of the implementation of the programs in LICs may be warranted as many countries remain in programs for extended periods. Furthermore, it should be considered how to increase the Fund's catalytic role for other sources of financing and close cooperation with the World Bank, MDBs, and donors. The NBC stressed that strong safeguards, including robust program design and careful assessments of capacity to repay and to manage debt, are paramount against the credit risks that potentially higher access levels would create. The NBC underscored the importance of the self-sustainability of the Poverty Reduction and Growth Trust, which is an important prerequisite for any adjustments to the facilities.

FURTHER READING: IMF Executive Board Discusses 2018 Review of Facilities for Low-Income Countries   2018 Review of Facilities for Low-Income Countries

4 CAPACITY DEVELOPMENT

Capacity development, including technical assistance and training, is one of the three core pillars of the Fund's work. Its main objective is to help member countries build institutions and capacity necessary to formulate and implement sound economic and financial policies. While the Executive Board will formally discuss the 2018 Review of the Fund's Capacity Development Strategy later this year, staff from the IMF's Institute for Capacity Development briefed the Executive Board in the first half of 2018 on the ongoing review of the Fund's capacity development strategy and the progress made on recommendations from the 2013 review. The presentation focused on the methodology of the current review, its preliminary findings, and key emerging themes. The overarching objective of the 2018 review is to reinforce the effectiveness and impact of the Fund's capacity development.

The Executive Board also received regular briefings by staff from the Fund's functional departments on the ongoing delivery of capacity development. NBC countries contribute with financial resources and/or technical expertise to the Fund's capacity development work.

Further details on the Fund's work on capacity development can be found here.

5 Independent Evaluation Office

The IEO is the IMF's Independent Evaluation Office that was created in 2001. Its task is to conduct independent evaluations of the IMF's activities and policies. The objectives of the IEO is to contribute to the Fund's learning culture, strengthen the IMF's external credibility and to support the Executive Board's oversight responsibilities. The independence of the IEO is safeguarded through its terms of references which states that the IEO reports to the Board and not to management, that is free to decide on what topics to evaluate and that the IEO Director is free to manage the resources and personnel of the office. The IEO normally produces two full evaluation reports per year. The evaluations include recommendations that the Board and management consider; and the recommendations that the Board endorses will be followed up in an action plan from management.

5.1 IEO's evaluation on the IMF and Fragile States

CONTEXT: In April, the IEO evaluation "The IMF and Fragile States" was released. The evaluation assessed the IMF's engagement with countries in fragile and conflict-affected situations recognized the contributions that the IMF has made in fragile states, including helping to restore macroeconomic stability, build core macroeconomic policy institutions, and catalyze donor support. The IEO report found that the IMF on balance had performed its various roles quite effectively but that there are still areas of improvements and the work on fragile states could be further prioritized. To this end, the IEO made recommendations in the following areas: the adequacy of existing financing instruments; capacity development; country-specificity of IMF advice and conditionality; and collaboration with development partners in fragile states. It also included recommendations on management of human resources working with fragile states and the handling of security issues in high-risk locations.

NBC VIEW: The NBC welcomed the IEO evaluation of the Fund's engagement in fragile states and noted that IMF has made and continues to make important contributions in these countries. The NBC supported most of the recommendations of the report, but suggested that the recommendation to establish a new institutional mechanism and the recommendation to adapt the financial instruments should be further analyzed and build on existing work and practices.

FURTHER READING: IEO Evaluation: The IMF and Fragile States Statement by the Managing Director on the Independent Evaluation Office Report on the IMF and Fragile States

5.2 External Evaluation of the IEO

CONTEXT: Since the inception of the IEO, its work has been evaluated by an external evaluation panel periodically. In 2018, the third external evaluation of the IEO was completed and the report and its recommendations were discussed by the Board. The external evaluation of the IEO found satisfaction that the IEO is independent and that its reports are of high quality. However, the evaluation panel's view was that there is not enough traction of the IEO's work in the Fund and that the IEO could play a greater role in contributing to the learning culture of the IMF. The conclusion was that the problem with traction was three-fold and that a recommitment from the IMF Board, management, and the IEO itself was needed for the IEO to reach its full potential and for independent evaluation at the IMF to become more effective.

NBC VIEW: The NBC welcomed the evaluation of the IEO and broadly endorsed the recommendations. The NBC especially emphasized the role of the Board in ensuring implementation, including holding management to account. Furthermore, the NBC pointed to the importance of raising staff awareness about the IEO and the relationship between the IEO and management and staff be improved and that IEO do better in engaging with staff and management before, during, and after an evaluation.

FURTHER READING: IMF Executive Board Considers External Evaluation of the Independent Evaluation Office The External Evaluation of the IEO - Report

ABOUT

THE IMF's EXECUTIVE BOARD

The International Monetary Fund (IMF) has 189 member-countries. Its highest decision-making body is the Board of Governors where all countries are represented. The Board of Governors approves only a few of the Fund's major decisions and has delegated the rest of its decision-making powers to the IMF's Executive Board where all countries are represented by an Executive Director. Some of the Executive Board's 24 chairs are single-country chairs, whereas the majority of the chairs represent multi-country constituencies. The task of the Executive Board is to conduct the daily business of the IMF in all aspects of its work, including surveillance, lending, and capacity development. The Board normally takes decisions based on consensus, but in some cases formal votes are cast. Each member country's voting power is determined predominantly by its quota, and the quota in turn is calculated to reflect member countries' relative position in the world economy.

THE OFFICE OF THE NORDIC-BALTIC CONSTITUENCY

The Nordic-Baltic Constituency (NBC) comprises Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway and Sweden. The Office of the Nordic Baltic Constituency (ONBC) presents the views of our member countries in the Executive Board in close coordination with our national authorities. The office also regularly meets with representatives from the member countries' administrations or private delegations. All positions in the office rotate between the eight member-countries according to an agreed schedule and all countries are represented at all times. As of July 2018, our staff includes:

Thomas Östros	Executive Director, Sweden
Kimmo Virolainen	Alternate Executive Director, Finland
Rimtautas Bartkus	Senior Advisor, Lithuania
Gudrun S. Gunnarsdottir	Senior Advisor, Iceland
Tove Katrine Sand	Senior Advisor, Norway
Eve Anni	Advisor, Estonia
Thomas Pihl Gade	Advisor, Denmark
Agnija Jekabsone	Advisor, Latvia
Emelie Mannefred	Advisor, Sweden
Maria P. Marin	Administrative Assistant
Tammy Timko	Administrative Assistant

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