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The Fund's Mandate - The Future Financing Role - Reform Proposals

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The Fund's Mandate—The Future Financing Role: Reform Proposals

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EXECUTIVE SUMMARY

Motivation. The global crisis has underscored the need for effective global financial safety nets to protect countries with sound policy frameworks from adverse outcomes. Complementing the traditional crisis resolution role of the IMF, which has been instrumental during the recent crisis and is expected to remain dominant going forward, further strengthening instruments to prevent crises and mitigate contagion in systemic events would contribute to the IMF's mandate to secure global stability.

Evolutionary reforms. This paper proposes specific reforms of crisis prevention instruments, and separately presents further considerations for strengthening the IMF's toolkit for dealing with systemic crises. The proposals, which have benefited from feedback from policymakers and other stakeholders, build on last year's major overhaul of the IMF lending toolkit and the reform options considered earlier this year by the IMF Executive Board in the context of a broader review of the institution's mandate.

Crisis prevention instruments. The reforms—with proposed decisions to be circulated as a supplement to this paper—aim to broaden the availability of insurance instruments in a way that responds to the heterogeneity of countries' policies and circumstances.

- The *Flexible Credit Line* (FCL), which was introduced last year and is available to countries assessed to have very strong policies and not requiring (ex post) policy conditionality, is to be further refined by: (i) allowing this credit line to be open for one or two years—in the latter case, an interim assessment of continued qualification is required after one year; and (ii) removing the implicit access cap of 1000 percent of quota, allowing more flexible access consistent with countries' circumstances.
- A new *Precautionary Credit Line* (PCL) is proposed for countries with sound policies but that nonetheless do not qualify for the FCL. Similar to the FCL, the PCL would be approved based on qualification criteria; but it would also have streamlined ex post policy conditionality focusing on reducing any remaining vulnerabilities. Access would be capped at 1000 percent of quota for a period of between 12 and 24 months subject to semiannual assessments of continued qualification and performance consistent with the credit line's policy objectives.

Systemic crisis resolution. The paper discusses options to establish a mechanism for mitigating contagion during systemic events, such as the recent global financial crisis. A Global Stabilization Mechanism (GSM) would be activated only in systemic events with the aim of proactively channeling financial assistance to help countries cope with large-scale liquidity withdrawals. As efforts at preemptively resolving systemic events have a global public good character, predictability on how such events would be handled in the future would contribute to global financial stability. Under the GSM, the IMF would mount a comprehensive response to systemic events by (i) making unilateral offers to approve FCL arrangements for systemic qualifying countries, (ii) activating other liquidity instruments for countries with sound policies that do not qualify for the FCL, and (iii) adopting a range of other measures as appropriate, such as activation of the New Arrangements to Borrow to expand loanable resources and considering an increase in global liquidity through general allocations of Special Drawings Rights (SDR).