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THE ROLE OF THE INTERNATIONAL MONETARY FUND IN A CHANGING GLOBAL LANDSCAPE

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Let me start by thanking Chairman Himes, Ranking Member Barr, and distinguished members of the House Financial Services Subcommittee on National Security, International Development, and Monetary Policy, for inviting me to speak at this hearing on "The Role of the International Monetary Fund in a Changing Global Landscape."

My name is Daouda Sembene and I am a Distinguished Nonresident Fellow at the Center for Global Development. I am also the founder and CEO of AFRICATALYST, a global development advisory based in Africa. I previously spent most of my professional career at the International Monetary Fund, where I ultimately served as Executive Director representing 23 African countries on its executive board. During my tenure, I chaired the statutory board committee which is responsible for strengthening collaboration between the IMF and other international institutions, notably the World Bank Group, the United Nations, and WTO.

I am pleased to share with you this testimony, building on my personal experience and available evidence on the future of the IMF. I plan to center my remarks around the following messages:

- First, the IMF should play a central role in efforts to address global challenges such as climate change and pandemics, as part of its mandate of promoting global financial stability. In doing so, it should put a special focus on the world's most vulnerable countries where it can make the most difference.
- Second, the IMF need to adapt its business model and policies and better leverage partnerships with other multilateral institutions to be more effective amid an evolving landscape.
- Third, successfull IMF engagement with member countries hinges on timely support from its major shareholders, particularly the US. But it also requires holding IMF leadership accountable for institutional performance.

1. ADDRESSING GLOBAL CHALLENGES

The COVID-19 pandemic and the climate crisis illustrate the growing extent to which the stability of the global financial system is vulnerable to new types of threats such as public health emergencies and natural disasters. In my view, such global shocks—just to name a few—are among the biggest challenges facing the IMF in coming years and they warrant a greater role for the institution in the provision of global public goods.

How the IMF responded to the pandemic? Should it have attached more conditions to its emergency loans? Was the issuance of special drawing rights (SDRs) the right course of action amid the crisis? These are fair and legitimate questions we can and should debate.

But we should admit that answers to these questions are likely to be overshadowed by the uncertainty over the counterfactual situation. What would have happened if the institution didn't quickly pull the trigger. Would liquidity shortages have translated into more solvency crises, leading more countries to default on their debt? Hard to tell.

Personally, I felt that the IMF did a great job of making additional liquidity available to its member countries. Since the crisis hit in 2020, new concessional commitments of about $ 9 billion were made by the IMF, including over $6 billion to Africa. In total, the IMF approved over 25 billion in emergency financing for Sub-Saharan Africa. This effort was unprecedented in the history of the institution.

But we need to put IMF support for developing countries into perspective. During the same period, total financial assistance extended by the IMF totaled about US$ 170 billion. Overall, the IMF made about $250 billion, a quarter of its $1 trillion lending capacity, available to member countries under its various lending facilities and debt service relief.

Moreover, by promptly acting as it did to support countries' efforts to respond to the pandemic crisis, the IMF has fulfilled part of its mandate which is to act as a lender of resort. At the onset of the crisis, access of African low- and middle-income countries to global financial markets was cut off, thus further reducing their already limited menu of financing options.

So, I think that the IMF's response was consistent with its remit and should be the norm, not the exception, in terms of crisis support for vulnerable low- and middle-income countries.

Preventing the economic disruptions of global poverty

A key responsibility of the IMF is to promote global financial stability and monetary cooperation. But the main purposes of the IMF, as defined under its Articles of Agreement, also include the need for the institution "to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members". The IMF has therefore a clear mandate to use its lending toolkit to help reduce global poverty and it has strived to fulfill this responsibility with mixed outcomes.

Paradoxically, IMF concessional lending in the pre-pandemic era has typically been quite limited compared to the extensive needs of developing countries. Its concessional window could only support, on a self-sustaining basis, an annual lending envelope of SDR 1.25 billion (about US$1.7 billion).[1] Still, the IMF continues to face persistent questions over whether it should act as an "aid agency" or a "development institution".

But to me the real question is more practical than ideological: it is how the IMF should act in an effective and timely manner, and in line with own mandate, to help address global poverty issues and avert their potential to undermine the international response to the global shocks like those I previously identified.

We are still witnessing how financing constraints and capacity weaknesses in the developing world pose a risk to the end of pandemic crisis and timely implementation of the Paris Agreement. The simple truth is that these global shocks cannot be sustainably overcome unless global development challenges that amplify them are concomitantly and forcefully addressed. And it makes natural sense to sustain the IMF contribution to these efforts, notably in terms of financial and technical assistance and/or policy advice.

Incidentally, it is worth noting that the IMF has long been involved in efforts by the international community to address priority issues that were presumably outside its core areas of competence. These include inequality, gender, climate change, corruption, digitalization, and Fintech. For instance, the executive board unanimously endorsed in April 2018 a framework for enhanced IMF engagement on governance and corruption Issues. The IMF's analytical work on gender has become a reference in the economic literature.

On the surface, these issues may be theoretically outside the IMF's core mandate but cannot be ignored by the institution because of their implications for economic and financial stability. So instead of eluding them, it makes more sense for the IMF to address them based on its own expertise, while building on the relevant expertise from other multilaterals.

It is worth noting that there are several ways the IMF can support the global development agenda without extending loans or issuing SDRs. These include developing technical and institutional capacities, supporting AML/CFT initiatives, monitoring risks to the economic outlook, and providing policy advice.

2. Institutional Reforms and Partnerships

What made the IMF continuously relevant since its inception was its ability to adjust to a new role and adapt to evolving circumstances and needs across its membership. This was the case in

[1] This traditionally limited IMF exposure is predicated on the notion that its loans are primarily meant to catalyze efforts to mobilize additional support from development partners.

1971 when the Bretton Woods system collapsed following President Nixon’s announcement of the suspension of the dollar's convertibility into gold.

This was also the case as the world continued to change afterward, notably with the combined effects of many developments, including the fourth industrial revolution and the 2008 global financial crisis.

Now we can expect the current pandemic to represent another inflexion point that warrants a new role for the IMF in support of global efforts to facilitate the delivery of essential global public goods.

Going forward, there is a continuous need for the IMF to adapt its business model and policies to the needs and circumstances of member countries. The IMF business model has been found to be inconsistent with the specific needs of some countries. For instance, evidence reported by the IMF watchdog—the Independent Evaluation Office—suggests that the institution provided a useful contribution in countries in fragile and conflict situations by promoting macroeconomic stability, catalyzing donor support, and strengthening institutions. Yet, some aspects of its business model were found ill-suited for these countries, including the short-term focus of the IMF’s financial toolkit and the quota-based access policies.

Let me now discuss a number of necessary IMF policy changes in no particular order of importance.

Greater IMF role in the provision of global public goods

Given the need for a greater IMF role in the provision of global public goods, I welcome the ongoing efforts by the institution to establish a $50-billion trust fund—the Resilience and Sustainability Trust—to help most vulnerable countries address longer-term structural challenges that entail significant macroeconomic risks to resilience and sustainability, including climate change, pandemic preparedness, and digitalization.

Clearly, the IMF alone will hardly be able to pull this off given its limited expertise on assessing climate risks. So, the reassurances provided by its management about the ongoing close collaboration maintained with the World Bank in the process of designing the RST are much welcome.

Personally, I am a firm believer that the IMF need to develop closer partnerships with other MDBs and regional development banks to better leverage existing SDRs. From my experience as a former chair of the IMF board committee in charge of collaboration with other multilateral institutions, I can tell you that such partnerships will not be concluded nor can they be sustained unless the heads of these institutions receive a strong mandate from their respective memberships and are held accountable for their performance on this front under a formal collaboration framework.

The IMF can play a constructive role in helping its vulnerable members address the challenges of climate change and public health emergencies by implementing sound and appropriate monetary and fiscal policy responses. But this will require strong country ownership of IMF-supported programs.

At the same time, IMF support should be tailored to the specific nature of these global public goods. When a country embarks on a program relationship with the IMF to build resilience to climate and public health shocks, it does so out of self-interest to achieve its own domestic goals. Nevertheless, its actions will also benefit the global community by securing progress toward global goals in these areas. As a result, RST financing should be extended to eligible vulnerable countries on highly concessional terms, notably through longer maturities and very low interest rates.

SDR reallocations

In August 2021, the IMF Board of Governors approved a general allocation of Special Drawing Rights (SDRs) equivalent to US$650 billion, which is the largest SDR allocation in the history of the IMF. Of this allocation, Africa received about US$33 billion. These resources significantly boosted official reserves and provided governments across the continent with potential additional financing to help achieve domestic priorities amid the pandemic crisis.

But the irony with the allocation of these SDRs is that countries that needed them most received the least, while those that did not need them secured the most. G7 and G20 countries secured about 280 billion and 440 billion worth of new SDRs, respectively.

Within Africa low-income countries secured about $6.5 billion, which is equivalent to 1 percent of the general allocations to IMF member countries and a bit less than 20 percent of the total amount allocated to Africa's 54 countries. The SDR allocation was welcomed in these countries. But the proceeds paled in comparison with their current financing needs. The IMF estimates that Africa's additional financing needs for COVID response will total about $285 billion through 2025, including $135 billion for low-income countries.

Over time, there is scope for thinking about ways to either make necessary adjustments to allocation rules to produce better outcomes or use more targeted SDR issuances for the benefit of countries in need. But in the immediate term, it is imperative to quickly fulfill the G20 pledge to mobilize $100 billion of voluntary SDR contributions for countries most in need.

IMF access policies

At the onset of the COVID-19 crisis, eighteen leaders of African and European countries and institutions jointly called for the IMF and other multilateral and regional institutions to "revisit access policies and quota limitations so that low-income countries can fully benefit from their support."

I fully share this view. In an CGD policy paper that I published last year, I urged the IMF to mobilize additional resources for its concessional window so that it can sustain, at least until full crisis recovery, the level of new concessional commitments that were made in 2020. I also called on the IMF to revisit its internal rules so that eligible African countries with sound debt indicators could potentially enjoy greater access to its nonconcessional funding in the event available concessional resources remains insufficient to close their external financing gap. Although access to nonconcessional resources is relatively more expensive, the reality is that such IMF lending is still generally associated with more favorable terms than many other loans currently available to these countries, including from global financial markets.

We should remember that when low-income countries' access to resources from the IMF and other multilateral lenders is inadequate, they usually have no other choice but to seek alternative—and oftentimes more expensive—financing sources. In many cases, this is often the price to pay to provide vital basic services to their population, preserve social cohesion, while addressing the severe security threats facing them.

Adjustment, Financing and Growth

Periodic reviews of IMF policies have led to marked improvements in the design of IMF-supported programs. I believe that there have been conscious efforts at the IMF to avoid *excessive* austerity. A recent report of the IMF watchdog concludes that there is no consistent bias towards excessive austerity in IMF-supported programs. The need to address the social and distributional consequences of adjustment has also been a recurrent theme in IMF board discussions.

But there is still evidence that the strength of fiscal consolidation requirements vary depending on the types of programs—that is concessional vs nonconcessional arrangements. In addition, IMF staff need to do a better job of assessing the implications of fiscal adjustment for growth. For instance, there are indications that IMF staff underestimated the negative growth impact in specific circumstances that increase the size of the multiplier, notably in weak economies and countries with fixed exchange rate regimes where the scope for using offsetting monetary or ER policy is limited.

To optimize the growth impact of adjustment, I believe that it is critical for the IMF to closely work with borrowing countries to:

- Ensure full country ownership of the adjustment and growth strategy;
- Better tailor the composition and pace of adjustment path to country specific circumstances;
- Optimize the growth payoffs of structural reforms;
- Better understand, monitor and address the social and distributional consequences of adjustment.

My sense is IMF's response to economic crises has evolved over time. Although IMF programs typically build on a mix of financing and adjustment, it seems to me that there was a tendency to rely disproportionately on adjustment during earlier crises. By contrast, there has been greater reliance on financing during recent crises, notably the COVID-19 pandemic.

3. THE ROLE OF THE UNITED STATES

Recent global trends pose several potential threats to an even and sustainable COVID-19 recovery and the stability of the global financial system, including increasing global poverty, rising inequality, growing debt vulnerabilities, the increasing prevalence of natural disasters and frequency of public health emergencies. For the IMF to be effective in helping overcome these threats, effective and timely from the US will be critical.

Let me give you a couple of examples.

SDR reallocation:

In the immediate future, the United States should play a leading role in ensuring prompt implementation of the G20 plan to recycle excess SDRs for the benefit of vulnerable countries. As recently noted by my former IMF board colleagues Meg Lundsager and Mark Sobel, the US Congress secure prompt approval of the Treasury's budget request to relend 15bn SDR, in addition to other possible resources for LIC support.

Time has come for the IMF membership to explore ways to innovatively use its toolkit to address global challenges, while building on its expertise and leveraging partnerships with other multilateral institutions, including MDBs. For instance, there is ample room for optimizing the impact of existing SDRs, while preserving their reserve asset characteristics. This includes not only strengthening global health security and supporting climate action, but also reducing debt vulnerabilities, particularly in emerging market and developing economies. This will require securing the 85 percent majority of the total voting power, putting the burden primarily on the United States and large shareholders. The US should also lead efforts to ensure that recycled SDRs are not exclusively used for IMF lending purposes. There is also merit in exploring ways to rechannel these resources through selected MDBs and regional banks such as the World Bank and the AfDB.

Debt vulnerabilities:

The COVID-19 pandemic has exacerbated existing debt vulnerabilities around the world, leading global debt to achieve record levels. In low-income countries, the World Bank estimates that debt rose 12%, reaching a record $860 billion in 2020, largely as a result of stimulus packages implemented at the onset of the pandemic.

Going forward, developing economies will continue to underperform their pre-pandemic levels due to inadequate access to vaccines and limited fiscal space. At the same time, output in advanced economies is on-track to reach its pre-pandemic trends as soon as next year.

In this context, the IMF and the World Bank played a welcome role in the formulation and implementation of the DSSI at the onset of the crisis. Since it took effect on May 1, 2020, the DSSI delivered more than $10.3 billion in relief to more than 40 eligible countries, including 32 African countries. Now that the DSSI has expired, liquidity-constrained and debt-distressed countries are currently left with no possibility of temporary debt relief.

The G20 Common Framework for debt treatment beyond the DSSI raised hope in many countries bending under the burden of debt, including the three countries that have already applied for it. But it has not yet delivered and will not reach its objectives so long as its current shortcomings are forcefully addressed. As suggested by the IMF and the World Bank, these include the lack of clarity on the different steps and timelines involving the process and on the methodological approach for assessing comparability of treatment. There will be limited incentives—if any—for any country to apply for it so long as it has not successfully dealt with at least one of the three cases at hand. Other eligible countries will think twice before applying given the potential risks of ratings downgrades and adverse market reaction.

So addressing these challenges will require an inclusive approach involving borrowers and both official and private creditors, all of whom stand to benefit from timely and effective debt restructuring. This begs the questions about what role the IMF should play in implementing G-20 common framework debt relief initiatives.

In my view, the IMF should engage both borrowers and creditors to ensure greater debt transparency. This is not only a requirement for adequate and reliable debt sustainability analyses, but also a critical prerequisite for any successful debt restructuring processes. Transparency in the debt restructuring process is critical to anchor expectations of participating actors and this role should be fulfilled by an independent party such as the IMF.

It is also the IMF responsibility to support efforts to ensure full participation and equitable treatment of creditors in the context of debt restructuring talks.

But time is of the essence. And the United States, China, and other G20 members should work collaboratively with borrowers, the IMF and all concerned stakeholders to quickly put in place realistic and workable debt restructuring mechanisms that produce fair debt treatments across bilateral, multilateral, and private creditors, while decisively helping countries in debt distress restore debt sustainability.