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The IMF's April 2024 Policy Reforms and Sovereign Debt Restructuring

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About the Author

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Acronyms and Abbreviations

AIP	Approval in Principle
CACs	collective action clauses
DSA	debt sustainability analysis
DSSI	Debt Service Suspension Initiative
G20	Group of Twenty
IMF	International Monetary Fund
LIA	Lending into Arrears
LIC-DSA	debt sustainability analysis for low-income countries
LIOA	Lending into Official Arrears
NTP	Nontoleration of Arrears Policy
OCC	official creditor committee

Executive Summary

The Common Framework for Sovereign Debt Restructuring provides a process for easing debt burdens on low-income countries but has operated too slowly for the four countries that have so far sought relief under it. Official bilateral creditors that are not members of the Paris Club are often principally responsible for the pace of the delivery of debt treatments. Under previous policies of the International Monetary Fund (IMF), recalcitrant official creditors have been able to slow the provision of financial assistance and extract concessions from other parties to debt restructuring negotiations. Recent changes in those policies are designed to expedite decision making and restrict the use of the approval process in this manner.

To remove speedbumps and veto points in lending to countries undergoing debt restructuring, the IMF in spring 2024 introduced changes to four policies and procedures: Lending into Official Arrears (LIOA), Financing Assurances, the Approval in Principle procedure (AIP) and emergency financing provisions. The Fund introduced a new, fourth channel through which it can lend into official arrears when, after due notice, no objection to doing so has been raised. A program can now proceed if Fund staff are confident that a "credible official creditor process" within key creditor governments will eventually provide a debt treatment consistent with program parameters, rather than relying on written promises. And the Executive Board can more readily approve a program in principle, subject to the subsequent provision of financing assurances, which maintains incentives in the interim for the borrower to prepare policy adjustments required under conditionality.

Although some observers would have preferred such reforms to have come earlier or would have preferred reforms that simplified Fund procedures (rather than making them more complicated), the current package has the virtue of being unanimously supported by the Executive Board, including representatives of newly emergent non-Paris Club creditors. The package holds the promise of accelerating the approval of IMF programs, thereby speeding financial assistance to debtor countries. These changes are not likely to overcome steadfast opposition to a program on the part of an important official creditor, but they incentivize would-be holdouts on the margin to cooperate. Reforms are likely to have their greatest impact in situations where a creditor is internally divided or needs more time to develop a common position among its various lending agencies; in such cases, the IMF can now advance programs where it would have previously been stymied.

Expediting and deepening sovereign debt restructuring also require reforms that go well beyond changes to IMF policies and procedures. But within the limits of what can be expected from the IMF, these changes are constructive. By reducing the time required to provide financial assistance, they are likely to contribute to an acceleration of debt restructuring and debtors' economic policy reforms, which will in turn limit economic pain and dislocation within the debtor country and curb financial losses on the part of official and private creditors.

Introduction

In April 2024, the IMF released changes to its policies and procedures that aim to remove speedbumps and obstacles in the way of lending in support of countries undergoing sovereign debt restructuring. Such lending is critically important to the orderly restructuring of debt and the pivotal role of the IMF in the debt restructuring process. These policies are prime examples of convoluted rules and methods that are nonetheless necessary for operating an official multilateral institution in a correspondingly complicated issue area, and this paper is intended to serve as a guide to understanding these reforms and provide an early assessment of their likely impact.

China's presence as the largest official bilateral creditor for many countries distinguishes the current situation from previous waves of sovereign debt crises. Its outsized role, as well as the prospect of other emerging market countries becoming large creditors in the near future, prompted the Group of Twenty (G20) to create the Common Framework for Sovereign Debt Restructuring beyond the DSSI[1] for low-income country cases to coordinate negotiations among official bilateral creditors in a

1 DSSI stands for Debt Service Suspension Initiative.

manner similar to the Paris Club's coordination of (mainly) advanced country creditors (G20 2020).[2] But negotiations, such as those over restructuring for Zambia and Ghana within the Common Framework and Suriname and Sri Lanka outside of it, have been prolonged and often fraught, which has delayed financial assistance from the IMF and the initiation of debtors' economic reforms. Such delays compound economic suffering in debtor countries and impose further, unnecessary losses on creditors. This experience prompted the IMF staff to establish a reform package, which the Executive Board ultimately approved.

The current reforms address several different policies and procedures of the IMF — Lending into Official Arrears, Financing Assurances, provisional Approval in Principle and emergency financing — which interact in complex ways. After first reviewing the institutional context and political economy of the IMF's role in sovereign debt restructuring, this paper discusses each reform in turn, identifying the change from previous arrangements. The concluding section then provides a preliminary assessment of the ability of these changes to speed delivery of financial assistance to restructuring countries and their other consequences.

The paper concludes, in a nutshell, that these reforms better equip the Fund to lend to countries undergoing debt restructuring and are likely to accelerate the approval of such financing. Within the scope of what can be expected from Fund procedures, these changes are quite constructive. Nonetheless, to render debt restructuring generally more responsive, thorough and timely, further changes in the architecture for sovereign debt restructuring beyond the ambit of the Fund need to be addressed.

The Fund's own document (IMF 2024a) provides an in-depth description of these reforms. The present paper develops the institutional context and political economy of IMF lending, elaborates further on the new changes, and can often be more explicit and direct than staff documents. It benefits from previous scholarship on the Fund's role in sovereign debt restructuring — including but by no means limited to Lee Buchheit et al. (2019), Guillaume Chabert, Martin Cerisola and Dalia Hakura (2022), Sean Hagan (2020), Gregory Makoff (2022), Theo Maret (2022), Brad W. Setser (2023), Mark Sobel (2022), as well as a podcast episode featuring Jeromin Zettelmeyer (Dauchy 2022) — and builds upon the author's CIGI policy brief published in October 2023 (Henning 2023a).[3]

These policies also interact with the Fund's guidance on the sharing of information (updated in June 2023), ongoing reform of the protocol for debt sustainability analysis for low-income countries (LIC-DSA) and the work of the Global Sovereign Debt Roundtable (see IMF 2023a, Setser 2024 and IMF 2024b, respectively). Owing to space limitations, further discussion of these policies is left to future papers for the time being.

Institutional Context and Political Economy

The policies of the IMF and changes to them are best understood in the context of the overall purposes of the Fund and the political economy of Fund lending.

Traditionally under the Paris Club and now under the Common Framework, debt restructuring requires that the debtor negotiate a program with the IMF. As part of program design, the Fund conducts a debt sustainability analysis (DSA), which, in combination with the macroeconomic framework and calculation of the financing gap, effectively establishes the magnitude of the debt treatment that is required to bring the country back to sustainability. That calculation effectively sets the minimum reduction of the debt that creditors must provide for the Fund to be willing to lend.

Once it lays down the size of the debt treatment, however, the IMF remains formally neutral with respect to how the losses are shared among creditors. Official bilateral creditors generally

2 The DSSI provided temporary relief from interest payments and principal repayments during the COVID-19 pandemic for requesting countries.

3 This paper uses the term "sovereign debt restructuring" broadly to refer to substantial modification of the financial terms of the obligations of national governments. It encompasses extension of maturities, reduction in interest rates and cuts to the face value of loans, bonds and other liabilities, even if the modification might be neutral in net-present-value terms. Debt in this context extends beyond the direct obligations of governments to also encompass liabilities of state-owned enterprises and sovereign guarantees of private companies.

insist on comparability of treatment among themselves and from private creditors, a matter that seems to be perennially controversial. But as far as the IMF is concerned legally, that is a matter for the creditors to negotiate among themselves and with the debtor country's finance minister. As long as their ultimate agreements satisfy the parameters of the program, including filling the financing gap, the IMF is officially agnostic on the distribution of sacrifice. This neutrality principle derives from the presence of various creditor states among the Fund's membership and an obligation not to take sides in disputes among members generally (IMF 1984; Ams et al. 2018, 1, 14), and, with respect to private creditors, not to interfere with contracts.[4] The principle places limits on the ability of the IMF to guide, referee or otherwise adjudicate the restructuring process.

Nonetheless, the IMF's lending decisions can strongly impact the incidence of loss and possibilities of recovery, not only among the debtor country and its creditors, but also among official and private creditors.[5] When a debtor country is in default or on the verge of it, its government is typically embroiled in a tug-of-war with creditors over repayments and debt relief. By lending, the Fund can give comfort and breathing room to the debtor, thereby relaxing its incentives to come to agreement with its creditors and potentially frustrating creditors' attempts to impose terms more favourable to them. By withholding lending until the debtor and its creditors agree on a restructuring plan, the Fund avoids tipping the scales in such negotiations. The prospect of an IMF loan that is conditional on a debt restructuring agreement serves as an incentive for debtor and creditors alike to come to the table and strike a bargain — although it is but one incentive among many other considerations and not necessarily decisive.

An essential element of the political economy of IMF lending, therefore, is the fact that the creditor countries that sit on its Executive Board and typically control most of the votes wish to avoid Fund programs' weakening their bargaining position with a sovereign debtor. Because these creditor countries also host international private banks, institutional investors and financial firms that may also be negotiating with the sovereign debtor, they have an interest in similarly protecting their private constituents, although they will typically place their own interests as official bilateral creditors ahead of those of private creditors. For this reason, the IMF adopted the position early on that it would not lend to a country that is in arrears to its creditors; it required that debts (before or after a restructuring) be serviced on a current basis.

In its original adoption, that Nontoleration of Arrears Policy (NTP) proved to be far too favourable to creditors, allowing (for example) private banks to force accommodation on the part of debtors as a condition for accessing IMF support in the 1980s. Beginning in 1989 and over subsequent decades, the policy was softened in stages, first with respect to private creditors (the Lending into Arrears Policy [LIA]) and then with respect to the official creditors themselves (the LIOA) (Lastra 2014, 63–65; Markoff 2022; Zettelmeyer 2022; Hagan 2022; IMF 2022, 2024a). Presently, the Fund applies a lower threshold to private creditors lending into arrears over official ones. Generally, the IMF can lend into arrears to private creditors if the borrower is engaged in good faith negotiations to restructure debt, whereas official creditors should explicitly agree at least in principle to restructure the borrower's debt along lines that are consistent with the program, embodied in a staff-level agreement with the borrower, before the Fund lends (unless some further stipulations can be met, as discussed below). The current reforms thus represent the latest stage in a decades-long trajectory of the NTP and LIOA policies that seek to preserve an active role for the Fund in debt restructuring cases, while navigating the demands and sensitivities of its creditor-country shareholders.

At the centre of discussions about the arrears policy is the question of how much leverage should be conceded to individual creditor governments over providing IMF loans to debtors. The ability to withhold consent to lending into official arrears gives creditor countries a great deal of leverage over the debtor in negotiations over the treatment of the debt as well as over other creditors, official and bilateral. A holdout creditor can use this leverage

4 The IMF can, however, offer its good offices to help resolve disputes among members.

5 There is an underlying central tension over the trade-off between adjustment and financing, with debtors generally preferring larger loans and more gradual adjustment and creditor countries preferring the opposite. This "austerity" debate pervades the work of the Fund but is not directly affected by the policy changes that are examined in this paper. The current policy changes instead engage the influence that the IMF has on the relative leverage of creditors and debtor countries that are negotiating a sovereign debt restructuring.

to extract concessions within these negotiations or potentially outside of them — for example, side deals in the area of trade, direct investment and foreign aid. And such leverage has been exploited, both in the past and more recently.

Key member states face an inter-creditor dynamic — a special case of the general collective action problem of creditor coordination in debt restructuring[6] — when deciding on the scope for IMF lending to a country that is running arrears with them. Specifically, there is a trade-off between preserving one's own prerogatives as an official bilateral creditor, on the one hand, and enabling a majority of official creditors to proceed with a restructuring over the objection of a minority holdout, on the other hand. By insisting on being able to block IMF lending oneself, a member state enables other official creditors to block such lending even when they might be minority holdouts, because the prerogative to veto must extend to all significant creditors in the Executive Board. By surrendering the option to singularly veto such a program, key member states would enable a majority of creditors to proceed with a restructuring, reducing opportunities for holdouts to extort side payments or block programs altogether.

The introduction of the LIOA policy in 2015 represented the latest formal attempt, prior to the current reform package, to widen the door to IMF lending into arrears over the objection of an important official creditor. It was done at that time to overcome Russia's effective veto of assistance to Ukraine. But the rise of China and other emerging creditors was already bringing into restructuring negotiations countries that were more, rather than less, inclined to protect an official creditor veto, which gave legacy creditors pause in further weakening their own veto prerogative. Accordingly, a 2021–2022 review of the policy specifically excluded reconsideration of lending into *official* bilateral arrears (IMF 2022).

As they relate to sovereign debt restructuring, the policies of the IMF can be understood in reference to three key elements of domestic bankruptcy proceedings: a stay of creditor action and standstill on repayments; debtor-in-possession financing to sustain regular operations; and cram-down procedures to resolve the holdout creditor problem. By replenishing foreign exchange reserves and government financial resources, IMF lending into official and private arrears serves the functional equivalent of debtor-in-possession financing. (Requiring debtors not to repay official holdout creditors until the latter agree to provide treatment that is comparable to that provided by a super-majority of creditors [Henning 2023a] serves as the rough equivalent of cram-down procedures and is analogous to CACs in private bond contracts.)

Two further observations about the IMF are useful to keep in mind. First, the formal policies of the Fund are proposed by staff and management and adopted by its Executive Board. As such, they provide an operational framework for the work of the staff and rules for making decisions on financing programs. They generally represent a consensus among the members of the Board on guardrails for the use of the Fund's resources, thereby carrying significant moral force and enabling them to exert a degree of constraint. But the Executive Board can also change policies as easily as it adopts them and has occasionally done so on the spur of the moment to remove contradictions with lending with which it is determined to proceed on other, pragmatic grounds.[7] Once the Board alters policy for a particular case, though, that change applies to all members and subsequent cases.

Second, the policies that are currently being reformed have arisen in the context of multiple institutions' involvement in sovereign debt restructuring, not just the IMF. Also engaged are the World Bank, especially in the case of low-income countries, and the Paris Club, as well as the Group of Seven and the G20.[8]

6 The dynamic is the same as that confronted by private creditors when introducing collective action clauses (CACs) into bond contracts. On the introduction of CACs in the wake of the Argentine crisis, see, among others, Makoff (2024).

7 A leading case in point is the introduction of the systemic exemption into the Exceptional Access Policy in order to pave the way for the Standby Arrangement for Greece in May 2010, notwithstanding serious doubts about debt sustainability. See, for example, Henning (2017, 86–91).

8 They constitute, in other words, an "international regime complex" for sovereign debt restructuring. See, for example, Henning and Pratt (2023).

The Elements of the Reform Package

Overall, the present set of changes is aimed at smoothing the pathway to releasing IMF resources to countries that are undergoing debt restructuring, after several bottlenecks and chokepoints were identified in recent cases. Softening or removing these obstacles involves changes in four policies or procedures of the Fund that are distinct yet related: LIOA; Financing Assurances; Approval in Principle programs; and emergency financing. In this section, each of these policies is considered in turn, with an assessment of their likely consequences.

LIOA

In 2022, the LIA policy (for private arrears) was reviewed and changed, but the LIOA (for official arrears) was not. Fund staff and the Executive Board have now addressed the latter in the latest review. This side of the policy is more sensitive owing to the fact that the official creditors, into whose arrears the Fund could be lending, are members of the IMF and sit on its Executive Board.

Prior to the current changes, there were three circumstances (now labelled "strands") under which the IMF could lend into arrears to official bilateral creditors, which continue to apply under the reformed LIOA policy. First, the Fund can lend when an agreement to restructure on the part of the Paris Club or another representative standing forum is in place. The IMF recognizes an agreement under the Common Framework, in which the Paris Club participates, as satisfying strand 1.[9] Second, the Fund can lend when the official creditor(s) provide consent, which represents strand 2. Note, however, that consent must be granted not only at approval but also at every subsequent program review. A creditor's ability to refuse renewal is a source of significant leverage, as suspension of the program would obviously be disruptive. Third (strand 3), the Fund can lend into official arrears if all of these three criteria are met: when prompt support is essential for a debtor; the debtor is making good faith efforts to negotiate with the creditor(s); and lending "would not have an undue negative effect on the IMF's ability to mobilize official financing packages in future cases." The third criterion was intended to avoid alienating large member-state shareholders that top up financing packages, which could jeopardize the mobilization of supplemental financing for future programs.

Thus, in practice under the LIOA policy preceding the recent changes, the IMF would not lend to a country in arrears to, say, the United States or Germany unless the Paris Club certified that it would provide a debt treatment in line with the requirements of the program. In the case of arrears to non-Paris Club creditors, such as China, the IMF would not lend unless an official creditor committee constituted under the Common Framework (which includes the Paris Club) commits to negotiating a debt restructuring agreement early in the program period, or unless China provides consent despite arrears, and proceeding would not jeopardize the creditor's supplementary financing for future programs.

The new changes introduce a fourth channel through which the IMF can lend into arrears to an official creditor: when a creditor has neither affirmatively consented nor objected to the program. The new change removes the simple failure of an official creditor to respond as an obstacle to lending. The Fund document refers to it as "strand 4," but here it can be referred to more descriptively as the "non-objection channel."

Under the non-objection channel, the IMF can proceed with a program and lend into arrears in the absence of receiving an outright objection provided that the other channels (strands 1–3) are blocked; a reasonable period of time has passed to allow official creditors to object; and the Fund can be sure that a sufficient proportion of arrears will be resolved in a manner consistent with the program on a timely basis. To satisfy itself of the latter — "safeguards" in the Fund's lexicon — the IMF staff would refer to the phasing of disbursements and conditionality of the program, commitments on the part of the debtor to negotiate with creditors in good faith, the inclusion of comparability of treatment provisions and commitments from a "sufficient set" of creditors to restructure.

9 In the lexicon of the Fund, there is a distinction between a "representative standing forum" and an "adequately representative agreement." The latter must cover at least a majority of official bilateral claims on the debtor over the program period. The Paris Club is the only representative standing forum that the Fund has officially recognized. An agreement struck by the Paris Club would not be "adequately representative" if it does not cover a majority of the claims, which would be the case when China or other non-Paris Club creditors hold the lion's share. But an agreement struck by an official creditor committee (OCC) in the context of the Common Framework does qualify as "adequately representative."

The rigour of these safeguards depends on whether the program provides the debtor with normal or exceptional access (that is, financing amounts that are several multiples of a borrower's quota). Standard safeguards would apply to normal access cases and would be satisfied by designing the program so that initial disbursements are limited in size, conditionality supports the restructuring process (such as through debt transparency and sharing of the details of negotiations with staff) and the debtor engages creditors in good faith. A commitment from the debtor not to service or redeem debt to an official holdout creditor until it agrees to comparable treatment[10] can be factored into the assessment of the debtor's good faith efforts, which the debtor is required to present in detail in a public letter (IMF 2024a, box 4, para. 21).

The IMF cites Suriname as a case in which a similar approach was applied. There, in December 2021, the Fund lent into arrears to official and private creditors with assurances from China and India that were "less specific than those provided by the Paris Club" but with their consent and indications that they intended to work toward a restructuring.[11] Staff also received assurances from the Surinamese government that it would secure comparable treatment from the holdout creditors before servicing obligations to them. Twenty-five months later, in March 2024, the Export-Import Bank of China finally agreed in principle to restructure on comparable terms (IMF 2024c, 57–61).

In cases of exceptional access, an additional set of safeguards would apply beyond those under the standard approach. This is referred to as the "enhanced safeguards approach." A program could proceed notwithstanding arrears when a "sufficient set" of creditors commit to restructure the debt in line with the IMF's macroeconomic parameters and DSA. Such a group will be deemed sufficient, going forward, when it has the participation of any qualified standing forum as well as "any creditors with significant influence over the debtor," which the Executive Board defines as having "the ability to extract repayment on more favourable terms, inconsistent with program parameters."[12] If China, India or Saudi Arabia held such sway over the debtor, for example, they would have to be party to such a commitment before the IMF could lend to a debtor in arrears under this non-objection channel. Fund staff cite Sri Lanka as just such a case, as it fell outside the Common Framework and negotiated with China separately from other official bilateral creditors.

Of the two levels of safeguards, the standard approach is the more innovative and permissive compared to prior practice because it reduces the threshold for lending. But even in cases of normal access, either a creditor or Fund staff can have the enhanced approach applied. This would happen if creditor coordination fails or a creditor or group of creditors is unable or refuses to provide the debt treatment required under the program, which would require facilitating creditor dialogue.[13] Under this scenario, the staff report would provide transparency into the negotiations by identifying the reasons the enhanced approach was invoked, the creditor(s) who invoked it, efforts made by creditors and why their coordination broke down (IMF 2024a, para. 20). Staff and the Executive Board calculate that such transparency will, at least in some cases, motivate greater cooperation among would-be holdouts.

One might question whether the IMF could get itself into a bind even under enhanced safeguards by lending into official arrears through the non-objection channel, if subsequent talks among official creditors descend into conflict and fail to produce a restructuring agreement. This situation could arise, among other possibilities, if Paris Club creditors suspect that a large non-Paris Club creditor was scheming to extract more generous terms or even full repayment under the table after the program was completed. Fund staff might recommend discontinuing the program (withholding further disbursements) as an inducement to the recalcitrant party to settle on common terms. But a decision to cut off the program could be complicated in the Executive Board, in which some directors could nonetheless be tempted to continue the program beyond the point where it should be suspended.

Perhaps anticipating such a scenario, the IMF report points out that staff can use the financing assurances review (see below) and a cap on

10 As advocated, for example, by Henning (2023a). See also Buchheit and Gulati (2022).

11 IMF (2021, paras. 19, 54–55 and 63). See also Maret (2023b).

12 IMF (2024a), Executive Board statement, para. 5, and staff report, para. 22.

13 Perhaps in combination with modifying the program, although this was not a scenario entertained in the staff report.

disbursements to limit the Fund's exposure to failures of creditors to agree. Identification of obstinate creditors under the enhanced approach's transparency would also tend to ward off this prospect. Disgruntled creditors should in principle have the ability to prevent continuance of the program by blocking the consensus by which the Executive Board generally makes such decisions. Given these considerations and that the proximate problem is delay of urgently needed programs (rather that perpetuation of insufficiently funded ones), this scenario seems to present a risk that is worth taking.

With these changes in place, most new programs for countries undergoing a debt restructuring can be expected to proceed through an agreement in principle on the part of an OCC under the Common Framework or a similarly representative forum (strand 1) or, alternatively, through the new non-objection channel (strand 4). Some programs may proceed through consent (strand 2), but these would probably involve countries with long-standing arrears or arrears in small amounts to relatively few countries and be correspondingly rare.[14] The criteria channel (strand 3) will also likely be little used.

The introduction of the non-objection channel is potentially consequential. There have been several occasions in recent years where programs have been held up for extended periods pending approval from creditor governments. Similar delays could be repeated with other countries, such as rising non-Paris Club creditors who have been slow to lay the domestic institutional neural pathways for decision making on restructuring. Because such delays are costly — for the country concerned as well as for other creditors involved — proceeding with a program can help to contain losses associated with debt unsustainability.

Financing Assurances

The IMF contributes only a portion of the total financing required under a program; supplementary sources are critical to its success in securing adjustment and restoring the country's access to international financial markets. When those sources fail to materialize, not only will the country risk failing to reach its targets, but its ability to repay the IMF could be jeopardized. Under the Financing Assurances policy, official bilateral creditors are required to provide "firm commitments" to fill any financing gap during the first 12 months of the program and "good prospects" that there will be adequate financing for the remainder of the program period. This requirement, which assures that the borrower has sufficient foreign exchange liquidity, applies to all programs.

When the borrower's debt is not sustainable, this policy carries the additional requirement that creditors commit to entering restructuring negotiations with a view to reaching agreement in line with program parameters prior to completion of the first or second program review. The additional requirement applies over a longer time horizon through the end of the full repayment period and ensures that the country is "solvent" and able to repay the IMF and other creditors.[15] Arrears to official creditors can be deemed to fill the financing gap, as can new credits on concessional terms.[16] Such assurances have normally been conveyed in writing, but have in some cases been delivered in a phone call between the prime minister or finance minister and the managing director of the IMF.[17]

However, in the cases of Suriname, Sri Lanka and Ghana, the financing assurances requirement became a source of considerable delay in advancing negotiations and a potential veto point in which a

14 In principle, it would have been desirable to align the consent channel (strand 2) with the safeguards under the non-objection channel (strand 4) by introducing the requirement that consenting countries also commit to restructuring debt along the parameters of the program. The absence of such a requirement has been a problem with reliance on the consent channel (see IMF 2024a, box 1). To the extent that strands 1 and 4 become the main channels through which programs proceed in the future, though, this omission would not appear to be particularly consequential.

15 The Fund refers to both the basic and additional requirements as "financing assurances," even though the latter apply only in debt restructuring cases.

16 One way in which the Financing Assurances and LIOA policies intersect.

17 Paris Club creditors indicate that they are willing to supply an "Agreed Minute," a collective restructuring agreement, while other official creditors indicate an equivalent willingness bilaterally. Non-Paris Club creditors' assurances must be from a "sufficiently high-ranking official authorized under domestic law to commit the creditor." Their statement should "preferably be written and must show an understanding of the debtor member's situation and the needed actions to restore debt sustainability in line with program parameters" (IMF 2022, 55–56, box AI.1).

creditor might have blocked a program altogether.[18] The procedures for providing assurances from the Paris Club had been well established, but the non-Paris Club creditors, such as China, were new to the process and communication between them and IMF staff sometimes fell short of what could be construed as "specific and credible," the standard applied by the Fund. In the case of Sri Lanka, staff went back and forth with officials from the Export-Import Bank of China and Chinese authorities several times in late 2022 and early 2023 before they had sufficient confidence in the Chinese commitment to a restructuring that would be consistent with the financing needs of the program (Maret 2023a).

To remove these obstacles, this paper's author (Henning 2023a) recommended that staff be given greater discretion in deciding what exactly constitutes sufficient financing assurances, so that they can finalize a program and present it to the Executive Board even when a holdout official creditor might be ambiguous about what it is willing to provide, and be mandated to report more fully and openly on conversations with creditors in each program review.[19] Buchheit (2023) went further, advocating the abolition of the financing assurances policy altogether; he argued instead that the IMF could simply withhold disbursements during reviews if not satisfied with creditors' promises to contribute.

The Fund has predictably chosen to retain the policy but has smoothed the path for approving programs in another way. In order to transcend dickering over the particular form and wording by which assurances are provided, the staff proposed to reorient its assessment toward an evaluation of the process by which official creditors make such decisions. This evaluation will hinge in large measure on a clear understanding of who within the creditor government makes the decisions that relate to assurances, information that they need, steps involved in that process and timelines for making the decision and delivering financing and/or debt relief. The official creditor's track record on previous cases will fundamentally inform this evaluation.

These changes can allow a program to go forward in the absence of a phone conversation or letter that provides specific and credible assurances, if Fund staff are satisfied that such a "credible official creditor process" is in place that will subsequently provide requisite assurances and eventually relief (IMF 2024a, paras. 27–35). Such cases could include instances where the official creditor is in the process of approving but for one reason or another is not proceeding under the timeline of the IMF for the purposes of the program. Fund staff would not have to wait on a formal decision of China's State Council (to cite a relevant example) if they could be assured informally that it will be forthcoming and such assurances have been fulfilled in similar cases in the past. The reform would not allow a program to go forward when an official creditor explicitly refuses to provide necessary assurances. Nor does the shift to evaluating creditor process affect the IMF's treatment of private creditors.

The Fund has also decided to make the treatment of financial assurances more detailed and complete in program reviews, which are public. Under previous practice, treatments of financing assurances in most reviews have been relatively thin. Going forward, the original staff report and subsequent reviews should provide an indicative timeline that is specific about the further steps required, including which creditors should provide any further assurances and whether the restructuring is taking place under the Paris Club, the Common Framework or another process.[20]

Importantly, in the absence of a response to a request for consent or financing assurances on the part of an official creditor, these reforms shift the right of initiative. With these changes in place, staff can initiate and the Board can approve such programs more readily. It is important to emphasize that the determined opposition of a large creditor and important shareholder can still block lending into official arrears. But to the extent that holdups might owe to a lack of prioritization of the decision or internal disorganization on the part of the creditor, the shift of initiative can be consequential.

18 In these cases, Chinese lenders delayed the initiation of IMF programs by several months, although there can also be other sources of delay. In the case of Suriname, for example, listen to Zettelmeyer (Dauchy 2022, minute 16) and see Maret (2023b). Ferry and Zeitz (2022) and Ballard-Rosa, Mosley and Rosendorff (2024) show that IMF programs generally take longer to negotiate when China is a large creditor to the country concerned.

19 The Executive Board amended the Financing Assurances policy in March 2023 in order to speed resources to Ukraine. The changes apply to cases of exceptionally high uncertainty and provide for official bilateral creditors to pledge at the outset to cover a borrower's obligation to the Fund via additional financing or further debt relief if one of these prove necessary (IMF 2023b).

20 IMF (2024a) para. 25, and summary of Executive Board discussion, paras. 8–10.

Approval in Principle Procedure

Notwithstanding the introduction of the nonobjection channel and changes to the financing assurances policy, delays in receipt of creditors' assurances can nonetheless arise under that channel (strand 4) or the representative forum channel (strand 1) when the Common Framework's OCC is slow. Such delays, coming between staff-level agreement and Executive Board approval of the program, can be costly if they are prolonged, as the program is in limbo in the interim. The borrower often puts off reforms until final approval, and the IMF's engagement, in terms of providing information and monitoring economic conditions, is constrained. If the delay is extended, program parameters might have to be recalculated in order to take account of what is usually a further deterioration of the country's economic circumstances during the intervening period.

To avoid such a situation, the new reforms have revived and amended a procedural tool referred to as AIP. The procedure provides for a decision by the Executive Board to approve a program, including all the usual elements of financing and conditionality, subject to the subsequent receipt of financing assurances. Once such assurances are received — in the form of a specific and credible commitment on the part of official creditors to negotiate a debt treatment in line with the program parameters[21] — the program can then take effect as designed. A second decision by the Executive Board is required to proceed with the program and the first disbursement.

This procedure dates from the 1980s, when it was adopted for programs that addressed the debt crisis of that decade. Its first use was for Sudan in 1983, after which it was employed in 18 other programs for countries in Africa and Latin America as well as for Yugoslavia. Its most consequential use was probably for the third Greek program during the euro crisis in 2017 (IMF 2024a, 51–53). In the Greek case, the IMF withheld its financial contribution to the troika program (IMF 2017a), which was mainly financed by the European Stability Mechanism, pending a debt treatment by official creditors. But the governments of the euro area refused to restructure on the Fund's terms and the provisional program was never activated. Nonetheless, the use of AIP allowed the IMF to shape conditionality, provide analysis and otherwise fully participate in the troika (Henning 2017, 201–32; IMF 2017b).[22]

The current amendments to AIP are aimed at allowing the procedure to bridge a longer time period between staff-level agreement and putting the program into effect than had previously been possible, thereby giving official creditors more time to sort out the treatment to be provided. The first Executive Board decision would be based on a fully negotiated program and would specify a date on which the approval in principle would lapse, set the time frame and circumstances under which it might be renewed and identify any other safeguards that the board wishes to apply (IMF 2024a, 26–28).

Under AIP, IMF staff can engage more actively with the debtor than the Fund would otherwise be able to do between the staff-level agreement and board approval. On approval in principle, the government should follow through on prior actions and begin implementing the reform package required under the program. Without such approval, it is difficult to justify the need to address these reforms in the domestic political arena, including the legislature. Valuable time can be wasted in those circumstances. In addition, Fund staff can share more and more detailed information with the borrower between the first and second board decisions than it would in the absence of AIP.

In sum, as intended, the effect of these changes to AIP will enable it to be used more often and effectively. It will give time to creditors to provide assurances when time is needed, but also set deadlines for receiving them, with the intention of moving the process along, and offers opportunities to the IMF to send signals to both the debtor and creditors about what will be necessary to meet program requirements.

21 The review of this commitment should include an assessment of the official creditor process.

22 The Greek debt restructuring of 2012, the largest to date, covered privately held debt and was accompanied by the very large amounts of official financing. Official claims on Greece were not restructured at that time, though they were reprofiled during the country's third program. Whether deeper restructuring of official claims was necessary was intensively debated, but the Greek economy has since grown faster than expected at that time.

Emergency Financing Provisions

The final part of the package addresses a gap in the arrears policy that arises when a member country is struck by an external shock that throws it into arrears and time does not allow for consultation and renegotiation with creditors. Under the previous LIOA policy, the IMF could determine that emergency conditions obtain and provide access to the Rapid Credit Facility or Rapid Financing Instrument notwithstanding arrears, without creditor consent or assessing whether the criteria channel (strand 3) applies. Under that scenario, however, financing should help the country normalize relations with official creditors and resolution of arrears.[23] But it was unclear exactly what circumstances constituted an emergency and which criteria guided assessment of progress toward normalization.

Under the present reforms, "exceptional circumstances" are clarified to be "natural disasters and a subset of other exogenous shocks, such as large or global shocks." The advancement of normalization is evidenced by the debtor's commitment to good faith efforts and promotion of creditor coordination. Such circumstances would not apply to a situation in which the debtor has already been in arrears for a long period, and the provision of finance through this channel should not undermine efforts to secure a full, regular program for a country (which large-scale financing or long-duration lending might do).[24]

Assessment and Conclusion

Collectively, how important is this package of reforms? The short answer is that it is very important to the IMF's expeditious administration of programs in cases where debt is not sustainable, and it will probably help countries receive debt treatments in a more timely fashion and thus also limit creditors' losses over the longer term.

A longer answer would acknowledge that these policies might have been amended differently. First, changes to LIOA could have been reviewed and introduced earlier, when the problems with integrating newly emergent creditors into the existing process first became apparent. Second, it would have been somewhat cleaner to simply eliminate the consent channel entirely and otherwise simplify these procedures rather than make them more complicated. Third, it would have been useful to make an explicit prohibition on servicing the debt of minority holdout official creditors a standard feature of programs for countries undergoing debt restructuring.[25]

But these additional measures might have raised the opposition of key members of the IMF and divided the Executive Board. Fund staff chose instead to pursue a consensus approach and succeeded in securing the unanimous approval of the 24 executive directors, including those representing large non-Paris Club creditors, thus preserving the unity of the board behind these reforms — a significant accomplishment. The measures that have been adopted are at the outer limit of what could be accomplished within the consensus among creditor member states on the board.

Taking a broader perspective, there is a limit to what can be expected from reforms of IMF policies and procedures with respect to the acceleration and deepening of sovereign debt restructuring. Changes to the policies and program-approval procedures at the Fund alone cannot overcome outright refusal on the part of creditors, official or private, to restructure debt or provide debt treatments on a multilateral basis. Nevertheless, within the scope of what we can justifiably expect from such policies, the package is constructive: it reduces several of the barriers to IMF support for countries undergoing debt restructuring that had been erected over the years to protect official bilateral creditors; and it narrows the scope for an outlying official bilateral creditor to use the IMF process to extract concessions that may be inimical to the interests of other creditors and the debtor.

Where an official bilateral creditor might be internally divided, domestically uncoordinated or simply in need of additional time to form an interagency position, the IMF can now advance

23 IMF (2015), summary of Executive Board discussion, pp. 4–5.

24 IMF (2015), summary of Executive Board discussion, para. 13.

25 See, again, Henning (2023a), among others.

programs where it would otherwise have been stymied. Some recent delays have been due to bureaucratic fragmentation within China and the incompleteness of internal coordinating mechanisms. (On China's internal organization, see Brautigam and Huang 2023; Jones and Hameiri 2021; Henning 2023b; and Chen 2023.) While assurances may come eventually, they would not come soon enough from the standpoint of the effective implementation of the debtor's program. Given the persistence of such fragmentation, as well as the strong possibility that it could be replicated in other newly emerging non-Paris Club creditors, lowering the threshold for approval of lending into official arrears has the potential to be quite important.

Perhaps most ambitiously, the package creates incentives for official creditors to develop their own decision-making processes to become more transparent, predictable and thus reliable in the provision of debt treatments. This applies to China as well as other emerging non-Paris Club creditors, such as those in the Persian Gulf. The biggest payoff would be in securing the convergence of domestic decision making of new and emergent creditors with processes long established within the member countries of the Paris Club. But this reform package can be beneficial, though less sweeping, in the absence of such convergence.

The next three or four cases of debt restructuring will reveal the extent to which the package can be described as a "game changer." In the meantime, the Fund will also review and revise its framework for analysis of debt sustainability.

However, expediting and deepening sovereign debt restructuring also require reforms that go well beyond changes to IMF policies and procedures. That agenda includes, but is not limited to:

- resolving issues such as comparability of treatment, inclusion of domestic debt, establishment of timelines, standstills at request and further improving debt transparency;
- extending the Common Framework or a similar arrangement to middle-income countries;
- enacting legal reforms, such as removing restructuring-hostile provisions in bond and loan contracts, limiting use of collateral and escrow accounts and introducing clauses that facilitate better risk sharing between creditors and debtors;
- resourcing and leveraging multilateral development banks; and
- more fully acknowledging the role of climate change and provisioning for global warming's impact on countries' debt-carrying capacity.

There is more work to be done.

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