Independent Evaluation Office
of the International Monetary Fund

IMF Response to the Financial and Economic Crisis: An IEO Assessment

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I. INTRODUCTION

1. The IEO is launching an evaluation of the IMF's response to the global financial and economic crisis, a natural follow up to the 2011 IEO report on *IMF Performance in the Run-Up to the Financial and Economic Crisis.* This evaluation will assess the IMF's actions in the wake of the Lehman collapse to help contain the crisis, cope with its impact on individual economies and financial markets, navigate a global recovery, and anticipate future risks.

2. The financial panic that followed the collapse of Lehman Brothers in September 2008 was contained as central banks provided massive liquidity to financial institutions and extended currency swaps to each other, while governments at the center of the crisis rescued systemic financial institutions. An economic rebound in 2010 from a sharp downturn in 2009 was, however, followed by slower global growth, and unemployment remains above pre-crisis levels in most advanced economies. Growth in emerging market economies also slowed after 2010, with many witnessing significant capital flow and exchange rate volatility. The IMF was involved in numerous aspects of the response to the crisis, including coordinating global and regional responses, channeling its surveillance into the recovery effort, and providing financial support to impacted countries.

3. The multi-faceted IMF response included the following:

(a) It served as a locus for international engagement and cooperation, in particular by facilitating a coordinated effort to contain the damage from the crisis, in which the Group of Twenty (G-20) assumed a prominent role.

(b) It called for significant fiscal stimulus in countries with fiscal space to counter the economic slump that would follow the Lehman collapse. Subsequently it recommended fiscal consolidation be initiated by 2010 or 2011 in major advanced economies.

(c) In collaboration with other global institutions, the IMF analyzed shortcomings in the financial sector policy and regulatory frameworks in major advanced economies and proposed corrective actions.

(d) It revamped its surveillance mechanisms to better detect prospective vulnerabilities as well as to assess the ongoing risks associated with the aftermath of the financial crisis.

(e) It bolstered its lending resources and made an allocation of SDRs to member countries. It introduced more flexibility in its lending instruments, increased access limits, and streamlined conditionality.

(f) It provided financial support to countries severely impacted by the crisis and facilitated a coordinated effort to limit the withdrawal of private financing in

Central and Eastern Europe. IMF lending increased from almost nil before the crisis to over US$200 billion in fiscal year 2011.

II. Objectives and Approach

4. The **objectives of the evaluation** are to assess the IMF's responses to the crisis and to identify lessons for responding to future crises. The evaluation will explore what worked well, where improvements may be feasible, and what lessons can be distilled on how the IMF operates at the multilateral and bilateral level, and across its areas of responsibility. The evaluation will examine the extent to which lessons from earlier crises were implemented. It will also assess the systems that the IMF has put in place to identify risk and vulnerabilities to prevent or mitigate future crises.

5. **Coverage.** The period covered will differ for different aspects of this evaluation. For most issues, the starting point will be the collapse of Lehman Brothers in September 2008, although in some instances it may be useful to assess events dating to the emergence of financial turbulence in August 2007. Similarly, the end point is likely to differ for different issues—balancing the need to produce useful and timely lessons, while making sure not to interfere with current operations of the Fund. For example, developments related to resource mobilization and the revamping of IMF facilities will be covered through 2012. On the other hand, the evaluation will not assess ongoing programs, nor will it cover programs in the Euro Area, which will be the topic of a separate IEO evaluation.

6. **Methods.** The evaluation team will gather information through a review of IMF documents and past and ongoing IEO evaluations, as well as documents from member countries, other international organizations, private sector research and investment outfits, and academia. Evidence will also be gathered through structured and semi-structured interviews with country authorities, Executive Directors, and current and former Management and staff. The evaluation team will also conduct interviews and organize workshops and seminars to elicit the views of colleagues from other international institutions, and private sector and civil society organizations.

III. Evaluation Questions and Scope

7. The evaluation will be organized around three areas of IMF activity in the crisis aftermath: coordination, surveillance and financial support to member countries. Key evaluation questions include the following:

(a) *On coordination.* What roles did the IMF play within the context of the global response to the crisis? What lessons can be drawn for its longer-term modus operandi? What are members' views on the IMF's post-crisis coordination role?

(b) *On surveillance.* Was IMF advice well founded and how effective was it in articulating measures to revive the global economy and promote financial sector reforms in impacted countries? Was the advice to shift from fiscal stimulus to consolidation timely? To what extent has the IMF's approach to risk assessment improved since the crisis?

(c) *On financial support.* Did the IMF coordinate/contribute to establishing an appropriate financial global safety net? Did it provide, or serve as a catalyst for, adequate and timely financial support to countries affected by the crisis? Was the associated conditionality appropriate?

8. Below are more detailed aspects of each of these areas that will be examined in the evaluation.

A. Coordination

9. The evaluation will consider the effectiveness of the IMF's actions to facilitate a coordinated response among national authorities, country groupings, and other international agencies. It will assess issues such as: the lessons that can be drawn by comparing "emergency" actions with the ongoing process of coordination; the modalities developed for cooperating with groupings such as the G-20 or the Financial Stability Board (FSB), and how potential trade-offs between traction and independence were handled; the perceptions of the broader IMF membership of the IMF's engagement with such groups; and the longer-term benefits and drawbacks of these modalities.

B. Surveillance

10. **IMF macroeconomic analysis and advice in the crisis aftermath.** The IMF's initial call for global fiscal stimulus and expansionary monetary policy was followed in 2010 by a call to shift to fiscal consolidation once the recovery was on a sustainable path, while relying on accommodative monetary policies including quantitative easing to stimulate demand, as needed in the face of fiscal restraint. The evaluation will examine the soundness and consistency of macroeconomic analysis and advice provided at the global level as well as at the country level, in particular for key systemically important economies. It will address issues such as: whether IMF advice was sufficiently differentiated across country circumstances; whether the IMF's recommended policy mix of fiscal consolidation and monetary accommodation in some advanced economies was well rationalized; whether cross-border spillovers of alternative policies were adequately discussed, and more broadly, whether the costs and risks of alternative policy options were appropriately weighed; whether there was consistency between the advice delivered and IMF analysis on related topics; and whether lessons from past financial crises were adequately absorbed.

11. **IMF engagement on financial sector issues.** In the crisis aftermath, the IMF (independently and as part of the FSB) had a prominent role in discussions on how best to

strengthen financial stability. The evaluation will describe the IMF's views on proposals to achieve the shared goals of making financial institutions and markets more transparent, less complex, and less leveraged. It will assess the proficiency with which the IMF analyzed key shortcomings of the pre-crisis regulatory framework and post-crisis restructuring and reform priorities. The evaluation will also discuss the IMF's progress in incorporating financial sector analysis into macroeconomic analysis in the context of both bilateral (FSAP and Article IV) and multilateral (GFSR and WEO) surveillance.

12. **Revamping early warning mechanisms.** The IMF significantly increased its focus on risk assessments following perceived shortcomings in its pre-crisis approaches. In addition to the vulnerability exercises for emerging market economies that were undertaken prior to the crisis, the IMF initiated vulnerability exercises for advanced economies and low-income countries. The IMF also introduced a semi-annual Early Warning Exercise, conducted in coordination with the FSB, to warn about systemic vulnerabilities and to discuss the policies needed to avert a crisis. In addition, a semi-annual Fiscal Monitor was introduced to complement the WEO and GFSR, annual spillover reports for five systemic economies were initiated in 2011, and a Consolidated Multilateral Surveillance Report was issued in 2011 and 2012. A risk assessment matrix and a debt sustainability analysis based on a revised framework are now included in bilateral surveillance. Finally, a high-level Surveillance Committee meets weekly in part to facilitate interdepartmental communication. The evaluation will describe the IMF's approach to assessing major risks to the global economy and the process of communicating these to the Executive Board, policymakers such as the IMFC, and the global community; and it will assess the strengths and weaknesses of the approach that has evolved.

C. Financial Support

13. **Resource mobilization.** At the outset of the crisis, IMF Management and member countries moved quickly to boost IMF lending resources to ensure adequate financing for the rapid expansion in anticipated requests for financial support. A tripling of IMF lending capacity was secured through ad hoc bilateral borrowing arrangements and an expanded and enhanced New Arrangements to Borrow (NAB). A doubling of quotas was agreed, but has yet to be effected. The evaluation will examine the multi-pronged strategy deployed to boost lending resources and assess its impact and implications.

14. **Revamping of lending facilities**. In 2009, the IMF overhauled its lending instruments, increased access limits, and streamlined conditionality. These changes included a new precautionary facility, the Flexible Credit Line (FCL), as a crisis prevention tool for countries with strong policies and performance track records. A Precautionary Credit Line (later the Precautionary and Liquidity Line) was added to the tool kit for countries deemed not to meet the FCL qualification standard. The evaluation will describe the evolution of post-crisis IMF lending instruments and changes to conditionality, and assess the underlying

changes that were made, drawing on the rationales provided by the IMF and the perspectives of country authorities.

15. **Assessing IMF programs in crisis-impacted economies.** The evaluation will assess the design, timeliness and outcomes of IMF-supported programs in countries affected by the crisis. The IMF's early post-crisis lending was centered on several countries in Central and Eastern Europe and Iceland. The evaluation will examine a sample of IMF programs from among these countries to assess the extent to which their design was well-calibrated to country circumstances and global or regional risk factors in the aftermath of the shocks experienced. It will also assess the effectiveness of the IMF's role in regional initiatives such as the Vienna Initiative to preserve commercial and other lines of credit following the sudden-stop in capital inflows.