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CHAIR IN SOVEREIGN DEBT AND FINANCE

FDL Finance for Development Lab

THE IMF'S EXCEPTIONAL ACCESS POLICY:

IT'S NOT WORKING

This note is a joint publication between the Finance for Development Lab and the Chair in Sovereign Debt and Finance at Sciences Po.

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Policy Note 21
January 2025

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Abstract

On December 12, 2024, the IMF's Internal Evaluation Office (IEO) released its evaluation of the IMF's exceptional access policy. Over the years, the IEO has delivered a number of well-informed and – on occasion – sharply critical evaluations of the IMF's activities, accompanied by recommendations that have had a meaningful impact on the IMF's reform agenda. Given the central role that the exceptional access policy plays in the IMF's lending activities, this evaluation is a particularly important one. The IEO's analysis of the application of the exceptional access policy amply supports its conclusion that the policy has not achieved its central objective. While many of the IEO's recommendations make sense, one of them – the introduction of an exceptional circumstances clause – is problematic. This note advocates for an additional reform feature, one designed to safeguard the IMF's catalytic role, while preserving flexibility. Specifically, it calls for the establishment of hard *ex ante* limits on exceptional access in "gray zone" cases; i.e., in those cases where the IMF does not have full confidence in the sustainability of the member's debt.

The Exceptional Access Policy: origins and objectives

Like many other IMF policy reforms in the area of crisis resolution, a key catalyst for the introduction of what is known as the "exceptional access policy" was a debt crisis in Argentina, this one being the collapse of the convertibility regime in 2001. As is described – in somewhat painful detail – in one of the IEO's first evaluations (conducted in 2004), the IMF had previously lent to Argentina amounts that far exceeded "normal" access limits in order to support an adjustment program that ultimately failed because, among other things, the IMF relied on excessively optimistic assumptions regarding the sustainability of Argentina's public debt. [1] (Normal access limits are calculated as a percentage of a member's "quota" in the IMF which, in turn, is based on the member's relative size in the world economy).[2]

The IMF's debacle in Argentina, coming on the heels of a number of large access programs during the 1990s, prompted the IMF to consider reforms that would impose greater discipline on its decision-making process. The reason why this reform was ultimately articulated in terms of access (i.e. the amount the IMF was willing to lend) is relatively straightforward: while IMF policies require that all programs have a reasonable chance of success, the risks to the IMF as a financial institution increase as the level of its exposure increases. And, critically, since the primary means by which the IMF mitigates this risk is by having confidence that the adjustment program will enable the country to service its debt to the IMF, it follows that the confidence level of program success should increase as IMF exposure increases.

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[1] The IMF and Argentina 1991-2001(2004)
https://www.imf.org/external/np/ieo/2004/arg/eng/pdf/report.pdf
[2] Current annual and cumulative "normal" access limits are 200 percent and 600 percent of quota, respectively. See, https://www.imf.org/en/News/Articles/2024/12/23/pr24499-imf-exec-board-concludes-2024-comprehensive-rev-general-resources-account-access-limits

It is important to recognize that the exceptional access policy operates within the context of a wider set of IMF lending objectives. Specifically, while the exceptional access framework seeks to manage the risk to the IMF as a financial institution, the overall objective of IMF lending is to help the member resolve its balance of payments problems "without resorting to measures destructive of national or international prosperity".3

This broader lending objective has shaped the overall design of the exceptional access framework in at least one fundamental respect: provided that the member's debt is judged sustainable and the adjustment program is strong, the IMF has been willing to take the risk of lending very large amounts - *with no ex-ante limits* - to help members address capital account crises without any mandatory participation from the private sector. While this approach creates financial risk for the IMF – and some degree of moral hazard - the view has been that avoiding a debt restructuring in these circumstances is of particular value to a member whose problem is judged to be that of illiquidity rather than unsustainability: it preserves its creditworthiness and avoids the short-term economic dislocation that would arise from an involuntary debt restructuring (particularly where the sovereign's claims are held in the banking system). Moreover, from the perspective of the international community, this approach –even if it means using IMF money to bail out private creditors - is often preferred since it avoids any contagion that may be created by a restructuring. [4]

This approach relies on the IMF's traditional catalytic role: it assumes that a sufficiently strong adjustment program, when coupled with IMF financial support, will generate enough market confidence to enable the member to borrow again at reasonable rates, thereby allowing it to refinance its maturing obligations. Moreover, it also generally assumes that a larger financial commitment by the IMF will be more catalytic since it signals greater IMF confidence in the program.

In contrast, where the member's debt is judged to be unsustainable, the IMF recognizes that the above approach cannot work since, in these circumstances, there is no feasible set of policies that will enable the member to service its debt under the original contractual terms. At this point, a debt restructuring is both necessary and inevitable. Indeed, in this situation, a decision by the IMF to support a program without a restructuring actually runs counter to the members' interests, and therefore the IMF's mandate, since it merely delays the inevitable and involves the member engaging in futile - and potentially harmful - adjustment measure to repay its debt.

Viewed from the above perspective, a key objective of the existing exceptional access framework can be understood as simply requiring greater evidence ex-ante that the program will work, and that the debt is sustainable. Stated differently, the objective is to replace a reliance on the type of unsupported optimism that gave rise to the failure in Argentina

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[3] IMF Articles of Agreement, Article I (v), https://www.imf.org/external/pubs/ft/aa/

[4] For a discussion of the costs and benefits of a debt restructuring in the context of the IMF's decision making process, see https://www.piie.com/publications/working-papers/sovereign-debt-restructuring-centrality-imfs-role

with a reliance on realism, to be achieved through a decision-making process that is based on a rigorous analytical examination of risks to the proposed program. As noted by the IEO in its current evaluation, when it was initially established, the policy sought to put in place “enhanced lending standards” by requiring “higher scrutiny” for cases where exceptional access was sought. [5]

Under the exceptional access policy, this exercise of discipline is achieved through the application of four criteria, all of which are, in effect, complementary metrics designed to assess the prospect of program success. Not surprisingly, the criterion that has received the greatest attention throughout the life of the policy is the requirement to determine debt sustainability. Consistent with the requirement of analytical rigor, the determination as to whether the debt sustainability criterion is met relies on the application of the IMF’s debt sustainability analysis (DSA), an analytical tool designed to determine the point at which a debt restructuring is judged to be necessary. Where debt is unsustainable, the DSA is also used to determine the overall quantum of debt relief that is needed. In these circumstances, the country can obtain an IMF program supported by exceptional access as long as it has initiated a restructuring process that delivers the necessary level of debt relief.

It should be emphasized that while the methodology underpinning the IMF’s DSA has become increasingly sophisticated over time, it still requires - as is noted by the IEO – the exercise of considerable discretion. In particular, a judgment as to the member’s debt service capacity requires an assessment of both a country’s future macroeconomic path (growth, interest rates, and exchange rates) and its ability to generate the necessary level of fiscal surpluses. This latter judgment, in turn, needs to take into account both economic considerations (at what point will growth prospects be undermined by tax increases and expenditure reduction?) and non-economic ones (does the government have the political capacity to push through necessary fiscal consolidation measures?). Notwithstanding the need for judgment, the DSA’s analytical framework, when taken together with the enhanced internal decision-making procedures established under the policy, is designed to constrain the exercise of discretion – and optimism.

As noted by the IEO, the evidentiary standards required for the sustainability criterion have evolved over the life of the policy. For example, while the general requirement has been that, *ex-ante*, debt sustainability be determined “with high probability”, the policy was amended in 2016 to enable the IMF to also provide financing in circumstances where debt was judged to be sustainable, but not with high probability- generally referred to as the “gray-zone cases”. Because of the higher risk of a future debt operation in these cases, the IMF could only proceed if the members also received financing from other creditors during the program. [6] This was designed to ensure that, in the event that a restructuring was needed, there would be an adequate pool of non-senior creditor claims that could absorb the burden of the debt operation. Importantly, this reform did not include the establishment of upper access limits in gray zone cases.

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[5] IEO Report, page 2
[6] IEO Report page 18

The IEO's findings: design vs. implementation

For purposes of its assessment, the IEO reviewed exceptional access programs over a 20-year period (2002-2023). The review included not only an analysis of the relevant internal confidential documents but also interviews with current and former IMF Executive Directors, management, and staff, as well as member country officials. Importantly, while exceptional access programs represented 30 percent of the programs approved during the relevant period, they represented 80 percent of the IMF resources disbursed, which gives one an idea of the magnitude of the IMF exposure with respect to these programs. [7]

Although the findings of the Report are nuanced in certain areas, the bottom-line assessment is relatively clear: the exceptional access policy, as applied, "has not enhanced the standards of IMF lending as envisaged".[8] Importantly, however, the conclusion that the policy has "not provided a substantively higher standard for exceptional access programs"[9] is not based on the fact that the program success rate for exceptional access programs was about the same as that for normal access programs. As is correctly noted by the IEO, such a comparison is not determinative, given the fact that countries needing exceptional access may often start from a more challenging position. Rather, the assessment is based on a determination that, ex-ante (i.e., at the time of the approval of the relevant arrangement), the IMF did not have a stronger analytical basis for greater confidence in program success in exceptional access cases relative to normal access cases.

The above conclusion is based in large part on an analysis of how the IMF's conditionality tools were applied in this context. These tools fall under two categories.

First, there is program design; i.e. to what extent is there a strong analytical basis to conclude that the economic adjustment measures envisaged under the program would, if implemented, resolve the member's problems? Stated differently, to what extent were assumptions grounded in realism rather than over-optimism? The IEO concluded that "while over-optimism in program growth and fiscal assumptions has long been a feature of IMF forecasts, it was more pronounced in [exceptional access] programs than [normal access] programs".[10] This finding is ironic given that a central objective of the policy was, in fact, to reduce over-optimism.

The second tool available to the IMF is program monitoring. Even if the IMF has a strong basis to conclude that the adjustment program, as designed, will fix the underlying problem, there is the risk that the country authorities will fail to implement it. To mitigate this risk, the IMF relies on measures that effectively release financing only if and when the necessary adjustment policies are actually introduced – most commonly through the phasing of disbursements based on the

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[7] IEO Report, page 6
[8] IEO Report, page 2
[9] IEO Report page 2
[10] IEO Report, page 23

satisfaction of key performance criteria. In circumstances where implementation risks are considered high, the IMF will rely on *prior actions*; i.e., it will not even approve the arrangement or complete a review unless certain policy measures are adopted. Given the objective of enhanced scrutiny and realism, one would expect that the use of prior actions in exceptional access cases would be higher than that in normal access programs. In fact, one of the IEO background papers concluded that "The number of [prior actions] did not differ much across [normal access] and [exceptional access] programs (…). Three-quarters of all program approvals and reviews of [exceptional access] programs had 2 or less [prior actions], marginally below the corresponding number of 3 or less [prior actions] for [normal access] programs."[11]

These findings raise an obvious question: why did the "stricter scrutiny" envisaged under the policy not materialize? Again, there is some nuance in the IEO's findings, which is appropriate given the fact that the circumstances of the relevant countries differed. Nevertheless, for a number of "high profile" cases, the message conveyed by a majority of IMF staff interviewed by the IEO is clear: as a matter of practice "[the exceptional access criteria] have not sufficed to shield the Fund the pressure in favor of lending when the fulfilment of the criteria is questionable".[12] This internal view is consistent with the perception outside the Fund "of political pressures in some high-profile cases affecting the assessment of EACs". [13]

Although not stated explicitly by the IEO, it is not difficult to deduce the reasons for this pressure: even in circumstances where there are serious questions regarding the sustainability of a country's debt, there is considerable pressure on the IMF to *avoid* making a debt restructuring a condition for its lending. Indeed, as noted by the IEO, debt restructurings were a relatively rare feature of exceptional access cases. The pressure on staff and Management comes from different stakeholders: even though a restructuring may be in the interests of the country in the medium term, it is likely to create short-term economic dislocation and, accordingly, political instability – indeed, it may cost the Minister of Finance his or her job. Not surprisingly, creditors whose claims are coming due would prefer to be bailed out by the IMF. And, as was illustrated in the case of Greece, concerns regarding the contagion may cause other countries to exert pressure to avoid making a restructuring a condition for its lending.

Of course, given the design of the exceptional access policy, this pressure fell heaviest on the application of the second criterion ("EAC 2"), which involves the application of the IMF's DSA. As noted by the IEO, "overoptimistic assumptions help to improve the consistency of DSAs with EAC2, reducing the need for debt restructuring before EA could proceed".[14] As noted by the

[11] IEO, "IMF Exceptional Access Policy; Exceptional Access Criteria Part I: EAC 1 and EAC4", page 21
[12] IEO Report page 27
[13] IEO Report, page 26
[14] IEO Report, page 23

IEO, "if macroeconomic projections and DSAs are optimistic, Fund access effectively becomes a substitute for necessary restructuring."[15]

The IEO makes an additional observation that is particularly troubling: exceptional access programs have "generally been ineffective in catalyzing private capital inflows".[16] In fact, the IEO found that the catalytic effect was weaker for exceptional access programs than for normal access programs.[17] This outcome is not only inconsistent with the objectives of the exceptional access policy, but is inconsistent with the objective of IMF financing more generally: for emerging market economies whose balance of payments problems arise from a loss of market access, regaining such access is a necessary means of achieving medium-term sustainability. Given the IEOs' finding – noted above - that a number of exceptional access programs were exceptionally optimistic regarding debt sustainability, this outcome is not surprising. Specifically, if there is continued uncertainty regarding the sustainability of a country's debt, a large amount of financing by the IMF will deter private inflows since private creditors are fearful of being subordinated to the IMF (as a preferred creditor) in the event of a future – and potentially very likely - debt restructuring. Moreover, to the extent that this fear of future subordination results in higher spreads, it actually increases the risk of default.

The IEO's recommendations: helpful with one important exception

The recommendations included in IEO evaluations, although not binding, are typically given considerable weight by the IMF's Executive Board. In this particular evaluation, the IEO does not call for a wholesale reconsideration of the policy's design. Rather, it recommends, among other things, that the existing framework – including the four criteria – be maintained but bolstered by the inclusion of guidance that provides greater clarity and specificity as to the meaning of the criteria and how they should be applied. This would be achieved by either modifying the text of the criteria themselves or by the inclusion of supplementary guidance for staff. [18]

These revisions would be helpful. For example, it would be very useful to provide further specificity and transparency as to the factors that are used to determine when a member falls into the "gray zone" (i.e., where debt is sustainable but not with high probability) and to develop better metrics for assessing prospects for regaining market access. In addition, as suggested by the IEO, there should be a greater focus on the risks associated with program design, not just program implementation.

On the other hand, its recommendation to introduce an "exceptional circumstances" clause would be problematic. In those circumstances where a program does not meet the standards of the four criteria – as bolstered by the additional specificity recommended by the IEO – the report recommends that the program still be approved on the basis of an "exceptional circumstances" clause that would be relied upon in "rare, well-justified cases, with adequate safeguards, including

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[15] IEO Report, page 23 (quoting Background Paper)
[16] IEO Report, page 2
[17] IEO Report, page 24
[18] The full list of recommendations can be found on pages 40-43 of the IEO Report

a strong program and possible additional third-party safeguards, and with clear disclosure of enterprise risks to the Board".[19] Presumably, the inclusion of such an exceptional circumstances clause would enable the IMF to apply, as a matter of practice, a true "strict scrutiny" standard to the rest of its programs. Of course, to the extent to which pressure is a significant part of the problem, the risk is that the use of the exceptional circumstances clause becomes anything but "rare", particularly if the additional guidance to be provided to staff – as advocated by the IEO – gives them less wiggle room in non-exceptional cases,

More fundamentally, however, the problem with this exceptional circumstances clause is that, while it would make the decision-making process more transparent (staff would no longer have to try to justify the unjustifiable), it does little to actually help the member country. Indeed, it is likely to further complicate it: if, as noted earlier, a key objective of IMF financing is to catalyze a return of market confidence, it is very unlikely that the market will view the use of the exceptional circumstances clause as a vote of confidence by the IMF in the strength of the member's program. Indeed, one of the reasons why the IMF has generally refrained from seeking third-party assurances regarding repayment (which the IEO now suggests could be used to partially mitigate risk in "exceptional circumstances") is that – while it would protect the IMF's balance sheet – it would actually undermine the efforts of the country to regain market access.

An additional reform feature: access limits in defined circumstances

When considering the scope of needed reform of the exceptional access framework, it is important to recall that one of the assumptions that has always underpinned the catalytic approach – and the overall design of the exceptional access approach – *is that very large financing packages would enhance market confidence*. This is a key reason why there are no pre-specified upper limits under the exceptional access policy.

However, the application of the above approach over the past 20 years reveals that there is an additional factor that needs to be taken into account for purposes of any review of the exceptional access framework: at some point, IMF exposure becomes so large that it can actually undermine the catalytic approach. Because of its status as a preferred creditor, large exposure to the IMF may make private creditors fearful of providing new financing out of a fear that, in the context of a potential debt restructuring, they will effectively be subordinated to the IMF by virtue of its preferred creditor status; i.e., they will need to bear a larger burden of the required debt relief because IMF claims are shielded from the restructuring process. *Clearly, this fear will increase as uncertainty about debt sustainability rise.*

As noted above, this observation was made by the IEO in the context of its finding that exceptional access programs were less effective than normal access programs in catalyzing private inflows. It is also consistent with one of the key lessons drawn by the Ex-Post Evaluation made by the IMF in December 2022 with respect to its 2018-2021 program with

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[19] IEO Report page 4

Argentina, another program with Argentina that failed to achieve its objectives.[20] That program was supported by the IMF's largest stand-by arrangement in its history: after an augmentation in October 2018, access under the arrangement amounted to US$57 billion (1,227 percent of Argentina's IMF quota). The central objective of the program was to address what was perceived as a temporary liquidity shock by catalysing renewed capital inflows.[21] The ex-post evaluation drew a number of lessons from the failed program, including, not surprisingly, the "sharpening" of the exceptional access framework" and the "importance of laying out the analysis and risks underlying key judgments as fully as possible when applying the exceptional access framework".[22]

But, in addition, the ex-post evaluation also identified the problem of the size of IMF support, which, when coupled with the IMF's senior creditor status, made the overall approach self-defeating:

"The experience underscores the need for the Fund to take a stand on burden sharing when entering into exceptional access arrangements—being the largest and most senior creditor to a relatively large country is both exceptionally risky to the IMF and potentially self-defeating to the basic purpose of catalysing a return to market access."[23]

Importantly, in its discussion of the above report, the IMF Executive Board endorsed its key findings, including the lesson that "an appropriate burden sharing is needed when entering into exceptional access arrangements"[24]

One way to operationalize such a burden-sharing mechanism would be to establish a hard upper limit – expressed as a percentage of quota – on the amount of exceptional access that a member can obtain from the IMF in "gray zone" cases, i.e., where the IMF does not have full confidence in the sustainability of the member's debt. Consistent with the approach used for establishing normal access limits, this upper limit would be established as a general policy and could be adjusted from time to time, taking into account the size of the IMF's financial firepower relative to total global capital flows. For requests that exceed normal access limits but fall below the "upper" exceptional access limit, the IMF's exceptional access policy would still require strict scrutiny.

By limiting the application of a hard ex-ante limit to gray zone cases, the IMF would be addressing those cases where there is the greatest risk of a future debt operation and, therefore, where there is the greatest risk of an "anti-catalytic" effect because of the higher likelihood of future subordination. (It is worth noting that, throughout the life of the program approved for Argentina in 2018, Argentina was classified in the "gray zone").[25] In contrast, where

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[20] Argentina: Ex Post Evalution of Exceptional Access Under the 2018 Stand-By Arrangement (December 2021)
[21] Argentina Ex-Post Evalution page 1
[22] Argentina Ex-Post Evaluation, page 3
[23] IMF Ex-Post Evaluation, page 4
[24] See Press Release attached to Argentina Ex-Post Evaluation Report, page 3.
[25] See Argentina Ex-Post Evaluation, page 48

the IMF has full confidence that the problem is one of liquidity (because debt is judged to be sustainable with high probability), the amount the IMF could lend would be unconstrained by *ex-ante* limits – but would continue to be subject to strict scrutiny.

Of course, for this approach to work, there would need to be confidence that the IMF would, as a matter of practice, be able to make the gray zone classification with the necessary degree of realism and analytical rigor; i.e., there would need to be confidence that the adoption of an upper limit would not result in cases simply migrating – as a result of pressure - to the "high probability" classification.

While this risk could be addressed by extending the scope of the hard cap to all requests for exceptional access, such an approach would come with a significant downside: avoidable debt restructurings would take place for pure illiquidity cases, with all of the attendant costs. It should also be noted that imposing a hard access limit in gray zone cases might also have the benefit of preventing another form of migration: for countries that are in the "red zone", the attraction of trying to be classified in the gray zone will be reduced because of the ex-ante limit.

A key issue will be the credibility of the hard limit. As noted above, it would be entirely appropriate for the IMF to review and adjust the upper limit from time to time based on general considerations (e.g., level of normal access limits and size of the IMF relative to global capital flows). What would be problematic, however, would be an adjustment made in the context of a request by a member that seeks IMF support at a level above the established limit. Unfortunately, and as pointed out by the IEO in an earlier evaluation, there is a precedent for this type of adjustment to the IMF's exceptional access framework: the introduction of a general "systemic exemption" that allowed the IMF to support Greece in 2012 in the absence of a finding that its debt was sustainable with high probability. [26]

One approach would be for the limit to be established -and adjusted- by the highest decision-making organ of the IMF, the Board of Governors. Although the Board of Governors has delegated general lending authority to the Executive Board, it has the legal authority to rescind this delegation and assume responsibility in this area at any time. In these cases, the Executive Board would be precluded from adjusting the cap in the context of the specific country requests.

Conclusion: the cost of maintaining the status quo

The merits of this proposed access feature should be weighed against the cost of maintaining the status quo. Continuing to provide unlimited amounts of financing in circumstances where there is considerable uncertainty regarding the sustainability of the member's debt not only undermines the effectiveness of that program but also undermines the general position of the IMF in at least two respects. First, as has been demonstrated on previous occasions

[26] This amendment was highlighted by a previous IEO Report that focused on the Eurozone crisis; see The IMF and the Crises in Greece, Ireland and Portugal (2016) https://www.elibrary.imf.org/display/book/9781475525144/9781475525144.xml

– the most noticeable one involving, again, Argentina [27] - when very large amounts that were lent by the IMF come due on the heels of an unsuccessful program, the IMF has come under tremendous pressure to approve a new program simply for the purpose of refinancing the amounts falling due to it. This pressure only further dilutes the quality of the adjustment program being supported, thereby further undermining the credibility of the Fund. Second, the status quo risks undermining the IMF's preferred creditor status: as IMF credit becomes an increasingly large portion of the debt stock, pressure from the private sector will grow for the IMF to participate in the debt restructuring process, particularly in circumstances where the level of subordination has increased because of a delay in the restructuring of a member's unsustainable debt.

[27] "IMF Approves Transitional Stand-by Credit Support for Argentina, January 24, 2003 https://www.imf.org/en/News/Articles/2015/09/14/01/49/pr0309