

GLOBAL ECONOMIC GOVERNANCE INITIATIVE

The Global Financial Safety Net Tracker: Lessons for the COVID-19 Crisis from a New Interactive Dataset

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SUMMARY

The world economy has gone into a freefall due to the COVID-19 pandemic. At the same time, policy-makers have a broader range of institutions to draw on for international liquidity support than before the global financial crisis 2008/09. Since the 2008/09 crisis, the so-called Global Financial Safety Net (GFSN) of institutions for short-term crisis finance has evolved into an uncoordinated patchwork of global, regional, and bi-lateral sources of support that lacks the resources to adequately prevent and mitigate the kinds of financial instability we are now witnessing.

According to estimates from a new interactive database compiled by the Latin American Institute at Freie Universität Berlin (LAI) and the Global Development Policy Center at Boston University (GDP Center), the financing available from the fledgling GFSN has reached about USD 3.5 trillion, or 4 percent of global GDP. Today, the IMF with its approximately USD 1 trillion lending capacity is by far not the only actor to provide emergency liquidity. Both regional financial arrangements (RFA) and bilateral currency swaps provide significant liquidity. While the level of support is larger than a decade ago, it is still less than one percent of total financial assets (FSB, 2020).

However, the distribution of availability of the GFSN is highly uneven and unequal, with many countries only having access to a relatively small portion of the GFSN, and some having few options altogether. Our data show that in 2018, about half of the IMF member countries only had access to the IMF. This concerns predominantly Sub-Saharan Africa and most parts of Latin America. In contrast, most countries in Europe, Eurasia, and Southeast Asia have access to powerful regional funds and/or have access to US Federal Reserve or People's Bank of China swaps. This means these countries are much better equipped to weather sudden stops and liquidity crunches of the kind the world is currently experiencing.

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The GFSN should not only increase its loanable funds. There is also an urgent need to coordinate the different elements of the GFSN. The status quo fire power of the GFSN can be used in a fruitful manner only if the diverse actors can begin to cooperate on different levels, while preserving their respective policy autonomy. An important element for this coordination will be a transparent and accessible information structure on the new, complex GFSN. To aid in this effort, LAI and the GDP Center recently launched the Global Financial Safety Net Tracker.

Beyond the IMF: The global financial safety net today

The ongoing COVID-19 pandemic represents the greatest stress test for national health systems since the 1912 Pandemic Influenza. At the same time, it represents the latest stress test for the emergent GFSN. COVID-19 and the ensuing economic hardships brought on by the pandemic and government response it necessitates will especially impact emerging markets and developing countries. These countries are forced to confront an erosion of global demand, a dramatic fall in commodity prices, and a capital flow reversal of a magnitude that will put downward pressure on exchange rates and increase debt levels across the world. Until the beginning of April 2020, the estimated USD 100 billion (Georgieva 2020a) outflow of capital from emerging markets and developing countries occurred in less time than during the 2008/09 global financial crisis or the Asian financial crisis.

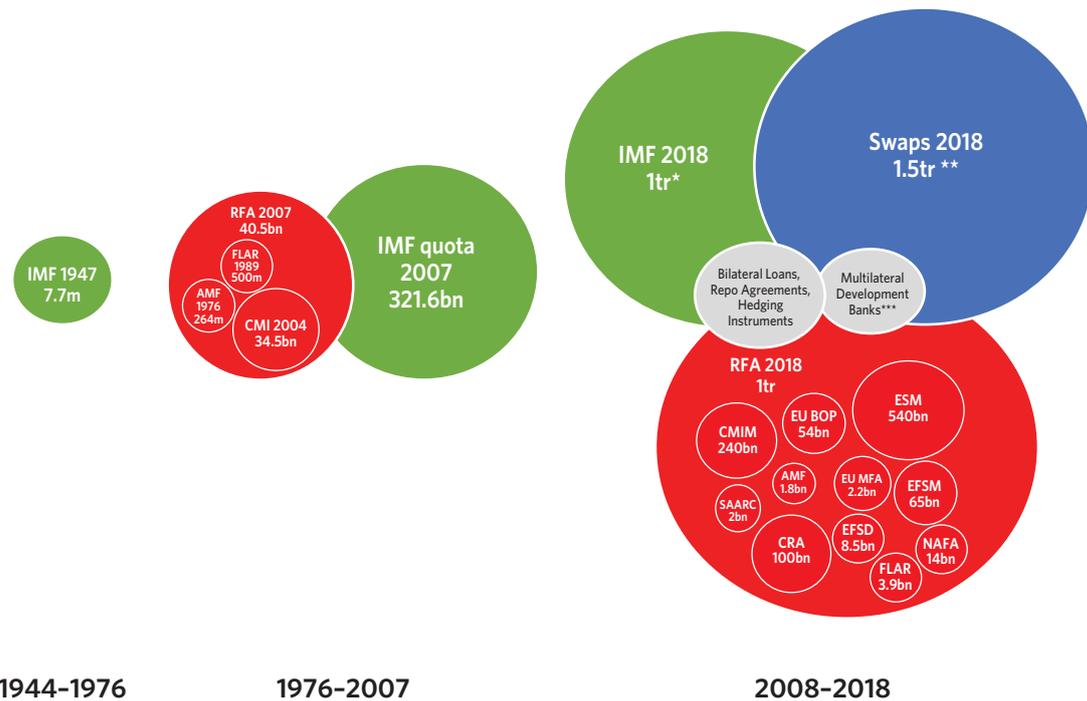
For a long time, the IMF was the only available source of financing for the majority of the world's countries. The first Regional Financial Arrangements (RFAs), the Arab Monetary Fund (AMF) and the Latin America Reserve Fund (FLAR), emerged in the 1970s as alternative lending sources. In part, their emergence represented reactions to oil price volatility and debt crises in North Africa and Latin America. The second wave of RFAs was created following the Asian financial crisis. Finally the global financial crisis provoked the creation of a number of diverse institutions that provide emergency liquidity at the multilateral, regional, and the bilateral levels. The regional funds in Europe (European Stabilization Mechanism, ESM), Eurasia (Eurasian Fund for Stabilization and Development, EFSM), and Southeast Asia (Chiang Mai Initiative Multilateralization, CMIM) were newly founded or enlarged in response to the 2008/09 global financial crisis. Today, the GFSN includes a large number of increasingly voluminous RFAs, bilateral currency swaps between central banks, crisis lending by multilateral development banks, bilateral short-term loans, repo agreements, and hedging instruments by central banks (figure 1).

Rather unnoticed by most, the GFSN has grown from one single global institution, the IMF, into a large and complex ecosystem of heterogeneous actors. Considering all these elements, the current GFSN capacity sums up to an estimated total lending capacity of about USD 3.5 trillion in 2018. This represents a more than tenfold increase of available short-term liquidity compared to the decades before the global financial crisis.

While this is a remarkable spike, it might not be enough to respond to a systemic financial crisis like the current one. Our calculation shows that out of the USD 3.5tr, about three quarters or USD 2.5 trillion, are designated to advanced economies. This means emerging markets and developing countries can only access a quarter of the total lending capacity.³ Hence, the GFSN currently does not meet the requirements to adequately respond to the financial necessities of emerging markets and developing countries resulting from COVID-19.

³ About USD 1tr is the estimated lending capacity based on paid-in quota in the IMF. At least half of the IMF lending capacity relates to quota paid in by advanced economies. About USD 1tr is the estimated lending capacity based on subscribed and paid in capital and/or quota in the RFAs whereof two thirds is the lending capacity for advanced economies (mainly through ESM, EFSM, EU BOP, partly CMIM and NAFA). About USD 1.5tr is the estimated active amount of currency swap lines in 2018 whereof more than three quarters is the liquidity of currency swaps between advanced economies - the bulk of it is the estimated figures for unlimited currency swaps of the Fed.

Figure 1: Institutions, agreements and size of the global financial safety net 1944-2018 in USD



Notes to this graph are listed at the end of the document.

Thus, when discussing the funds available to support countries to fight the spread of COVID-19 and its economic consequences, the GFSN has a much higher sum available than the much cited one trillion USD IMF lending. However, for emerging markets and developing countries, further efforts to increase total lending volume seem to be necessary: at the end of March 2020, IMF director Kristalina Georgieva (2020b) estimated the finance needs of emerging markets only to sum up to at least USD 2.5 trillion, for which their own reserves and domestic resources would not be sufficient.

Further, the total sum of the GFSN lending capacity could be borrowed and lend more effectively if the decentralized mechanisms on the global, regional, and bilateral level were coordinated. Several attempts to coordinate IMF and RFA activities have been made since the G20 called for enhanced collaboration (G20 2011, OECD 2019). However, a predictive and transparent joint GFSN system with its decentralized elements by integrating their several strengths and weaknesses is still missing, apart from some coordinated surveillance efforts between IMF and selected RFAs. Despite calls from the G20, IEO, and others for better coordination, the GFSN suffers from patchiness and unevenness. Coverage for individual countries varies with access to and volume of an RFA, or to currency swaps, among others (Mühlich/Fritz 2018). Thus while the GFSN has significantly more firepower to address the COVID-19 pandemic than during the 2008/09 global financial crisis, it appears to still fall short of potential borrowing needs. The more complex and dynamic GFSN “introduce[s] new types of inequities into the system, and coordination across a fragmented system toward common goals may prove to be difficult.” (Kring/Gallagher, 2019).

We calculate the individual short-term liquidity available – or ‘fire power’ – of IMF, RFA and swaps per each of the 189 IMF member countries in 2018 as a percentage of a country’s GDP. At the global level, we identify three groups of countries with very unequal access and borrowing options in the GFSN.

1. **Liquidity is largely concentrated in a handful of countries that are mainly advanced and emerging economies.** In terms of global GDP, about 20 percent of IMF member countries can be seen as over-insured in relative terms. They can resort to all elements of the GFSN: the IMF, their regional funds, and/or bilateral swap lines, usually with the US Federal Reserve Bank (Fed) or the Peoples Bank of China (PBOC). On average, GFSN coverage equals 8.5 percent of their GDP. In this group, we find a little more than half of the countries to be advanced economies and the other close to half to be emerging markets and developing countries. The group is made up of ECB member countries that have access to the ESM, but also Southeast Asian emerging markets such as Malaysia, Singapore, or Thailand that are members of the CMIM,⁴ and some developing countries that are member to the EFSD, such as Armenia, Belarus or Tajikistan.
2. **Almost half of the countries analyzed here have no further access to regional funds or swaps, so they have to rely exclusively on the IMF.** In comparison to the first group, this group is relatively under-insured. On average, these countries can draw 3.5 percent of short-term liquidity in terms of their GDP, less than half the amount that ‘over-insured’ countries can access. The majority of them are developing countries, and some emerging markets.
3. **About 30 percent of IMF member countries are excluded from currency swaps but are member countries of a regional fund.** However, with about 3.3 percent of GDP on average, their coverage of potential crisis finance needs is even less than that of countries with only IMF access. Most of these countries are relatively large member countries of smaller RFAs, such as the AMF or the FLAR, with only a few countries being small enough to find relevant coverage by their regional fund.

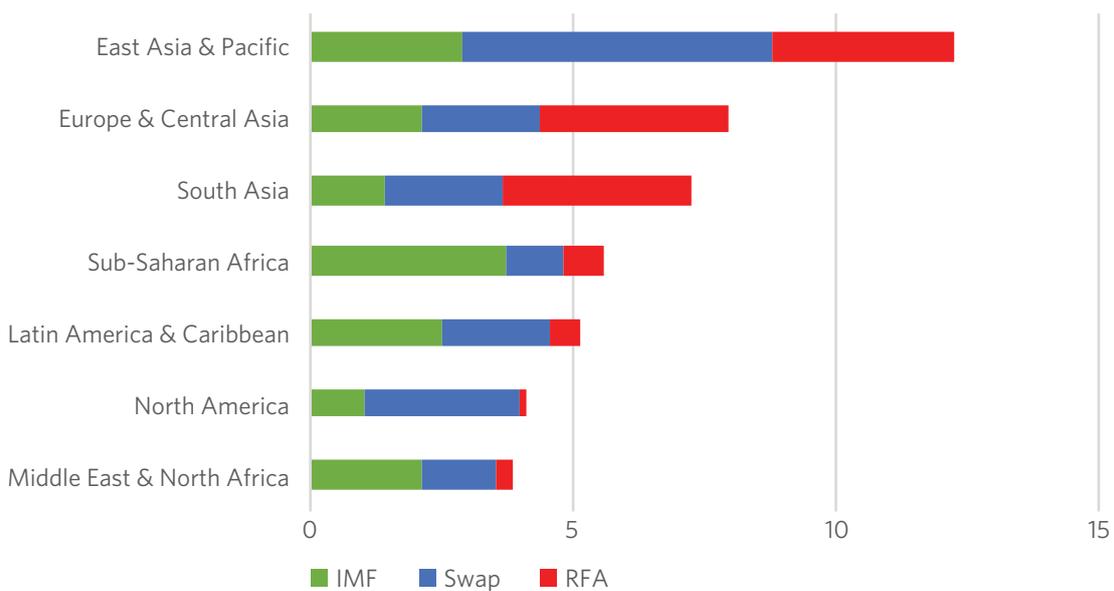
The analysis of the 2018 state of the art of the GFSN shows that regional funds and currency swaps make a huge difference especially for the one-fifth of IMF member countries that have access to both of them. On average, regional funds are able to provide about 149 percent of the IMF’s accessible ‘fire power’ for member countries of regional funds, while currency swaps can provide about 158 percent for those countries that partnered a currency swap. However, about half of the IMF member countries are excluded from these options.

Figure 2 shows the inequity in GFSN across different regions. We find that Sub-Saharan Africa is the region least covered by the GFSN. This is especially problematic for those countries that turned into frontier markets for international financial investment over the last decade. These countries currently require high financial volumes to cope with capital outflows. Further, low income developing countries concentrated in this region might rather need debt cancellation and grants. Also, Latin America, with its relatively small FLAR, and swaps exclusively offered by the Fed only to Brazil and Mexico, is under-insured as a region. In contrast, both the emerging markets in Southeast Asia and Central Asia, and the Euro member countries, mainly belong to the group of privileged over-insured countries, as they have access to relatively large RFAs and/or to swaps, provided by the PBOC in Southeast and Central Asia or by the Fed for Europe, Canada, and Japan.

Inequities in access to the GFSN entail several risks. First, for the underinsured countries, the lack of provision of sufficient emergency liquidity could potentially deepen and prolong a crisis and its economic and social costs. Prolonging a crisis often creates unintended spillover effects for neighboring countries. Second, those countries that have access to multiple layers of the GFSN also could incur potential risks.

⁴ This holds even if we count only the liquidity amount of the Southeast Asian CMIM and the BRICS’ countries’ CRA that is not linked to an obligatory IMF program.

Figure 2: Average available liquidity as share of GDP per region in 2018



Notes to this graph are listed at the end of the document.

For example, the costs of a crisis may increase due to lengthy negotiations during creditor shopping by the borrowing countries, and provoke moral hazard behavior and risk concentration in certain GFSN elements. On the other hand, the over-insured countries can leverage on the traditional IMF program by complementing (or even substituting) IMF lending with financing from other available GFSN elements, or by ‘bridging’ IMF programs with quickly available small regional fund programs (ESM 2018). Hence, maintaining choice and competition in the system is important to encourage better service delivery and enhance the bargaining power of governments regarding programs to return nations to stability and sustainability (Kentikelenis et al., 2016; Kring and Gallagher, 2019). At the same time, inequalities in access and available short-term financing point to the uncoordinated status quo of the GFSN. Most importantly, uncoordinated surveillance and lending entails the risk of mistakenly categorizing a solvency crisis as a liquidity crisis (see for a comprehensive discussion Henning 2020).

Rising to the Task of COVID-19

The present crisis of COVID-19 highlights the importance of a more robust, inclusive, and equitable GFSN. Analysis of the 2018 data suggests three policy recommendations:

First, the figures suggest the **need to level out the geographic coverage of the GFSN**. As our data reveals, almost 50 percent of the world’s economies only have access to one pillar of the GFSN – the IMF. Not only do these countries face limited crisis finance, in addition, they have to face lending programs that are subject to intensive debates about the adequacy of policy conditionality attached to them. Regional funds have been created as vital alternatives to the IMF. Even if many of them are small in size, these alternatives are a vivid source of emergency liquidity for many countries, especially the smaller ones (Mühlich/Fritz 2018). Regional funds play an important role in the new GFSN ecosystem of crisis prevention and backstop and should therefore be broadened and strengthened to ensure that each region has an expanded set of options in times of need (ESM 2018). The most glaring gap is in Africa, which however, has negotiated an African Monetary Fund that is in need of signature and ratification (Dagah et al, 2019).

Second, we see a **need to expand the resources of the GFSN**. First, the COVID-19 pandemic is likely to lead to a need for a significant increase in IMF and regional fund's lending volumes, especially for emerging markets and developing countries. As the anchor of the GFSN, the IMF will need to increase its lending volume and diversify its resources, such as through issuing a large volume of Special Drawing Rights (Gallagher et al. 2020). Smaller regional funds will need a stepwise scaling up as well.

Third, **a coordinated GFSN is a more effective crisis firefighter** and expanded coordination across all elements of the GFSN is long overdue. The status quo fire power of the GFSN can only be used in a fruitful manner if the diverse actors of the decentralized ecosystem come to terms with how to cooperate on different levels, while preserving their respective policy autonomy and comparative advantages. The IMF and the regional funds have only taken incremental steps towards a coordination framework despite calls for constructive engagement with the regions to develop a predictive and transparent joint system of surveillance and disbursement of crisis finance (EPG 2018, ESM 2018, IMF 2016, 2017).

Last but not least, the COVID-19 related crisis shows there are more players which need to be brought to the table for coordinating emergency liquidity at the global level. The swap providing central banks, especially the US Fed and the Chinese PBOC, have become game changers for the GFSN, and could do much in terms of increasing transparency, and coordinating liquidity in a more efficient manner, especially for the more vulnerable emerging markets and developing countries. "Further coordination among major central banks could help ease swap lines and provide liquidity in the financial system, especially in emerging economies and developing countries." (Guterres 2020)

The Interactive GFSN Tracker

To bolster efforts to coordinate the various layers of the GFSN, the Latin American Institute at Freie Universität Berlin (LAI) and the Global Economic Governance Initiative (GEGI) at the Global Development Policy Center recently launched the trial version of an interactive GFSN tracker that highlights the lending capacity of the IMF and RFAs (figure 3). Additionally, the tracker provides historical lending data for 50 emerging market and developing countries and 20 advanced economies that were members of an RFA between 2015 and 2017. For each country, the database shows any borrowing agreements with the IMF, an RFA and any bilateral currency swap agreements, irrespective of whether the agreed funds were indeed drawn.

We assume the agreed and available finance volume to show where the crisis-affected country sought liquidity, how it combined the different GFSN elements, etc. Further, an agreed and not necessarily drawn IMF or RFA loan or a swap agreement has a market signaling power (irrespective of its negative or positive nature) that we assume to have an effect on a crisis. Thereby, we visualize retrospectively the actual third-party crisis intervention, the changes in globally, regionally, and country-level available liquidity volumes over time and the difference between preventive loan agreements and actual liquidity utilized.

The GFSN tracker in its fully elaborated version will make existing GFSN data comparable (Scheubel/Stracca 2019; Mühlich/Fritz 2018; Denbee et al. 2016), while considerably amending them in real time as the crisis unfolds. We hope to track each new loan or swap across the GFSN and update that information for policy-makers, analysts, civil society, and journalists to be able to treble their responses in the near future. First, national foreign exchange reserves are not documented as a component of the GFSN. While scholarship commonly refers to foreign exchange reserves as a major component of the GFSN, standard economic literature shows that in all types of balance-of-payments crises in emerging markets and developing countries, the third-party actor must come from outside the country and provide timely, voluminous and smoothly-decided conditionality and decisive action to combat a crisis (Obstfeld 1996). Empirical investigations into the role of foreign exchange reserves as crisis prevention and backstop

Figure 3: Global Financial Safety Net Tracker



shows that the intervention of an external third-party actor is indispensable to backstop a financial crisis. In fact, regional funds and currency swaps dominate national foreign exchange reserve accumulation as a precautionary measure (Aizenman 2010, Aizenman et al. 2011). Foreign exchange reserves only work as crisis insurance when they are maintained, otherwise they will be rapidly depleted.

Second, in contrast to existing literature, we include the short-term lending by MDBs as they act at the margins between budget support and structural lending. This data is included in the historical data, but not in the overview of the RFA and IMF global lending capacity. Here, the correct identification of the nature and adequate response for a financial crisis in a coordinated way becomes visible as MDBs offer short-term liquidity and long-term structural finance (ADB 2019, Ulatov et al. 2019). Third, based on macroeconomic vulnerability indicators the GFSN tracker will enable to map vulnerability and the relative fire power of the GFSN in the same place for the first time.

The fully elaborated GFSN tracker provides insight to policy makers, academia, and others on emergency financing alternatives to the IMF. The tracker also helps identify gaps and inequities of the current GFSN, as it identifies, documents, and displays the scale, composition, and distribution of global liquidity resources. This will fill an important gap in our understanding of the GFSN's coverage that will help government institutions, policy-makers, as well as international organizations, think tanks, and researchers to better understand the scale and composition of the GFSN and to track and analyze the manifold opportunities, risks and changes of the GFSN in the future. The tracker can be used as an analytical tool to assess the functioning, coverage and utilization, including patterns of substitution and complementation of the GFSN elements for different countries, country groups, regions and the world. This information can provide grounds to develop country- and region-specific mechanisms of coordinated liquidity provision that attributes each element a certain role in the GFSN ecosystem to become predictive, transparent, disburse quicker with adequate volumes, and conditions to close gaps in crisis prevention and backstop.

NOTES

FIGURE 1

Source: Authors' compilation based on IMF 1947, 2007, 2008, 2018, n.d.a; FLAR 1989, 2018; AMF 1977, 2018; AMRO n.d.; Denbee et al. 2016, updated by Dennis Essers (Essers/Vincent 2017) and by the authors; Kawai/Houser 2007; BRICS 2014; EFSM n.d.a; ESM n.d.. AMF – Arab Monetary Fund; FLAR – Latin American Reserve Fund (according to its Spanish acronym); CRA – Contingent Reserve Arrangement of the New Development Bank; CMIM – Chiang Mai Initiative Multilateralization; SAARC – South Asian Association for Regional Cooperation Swap Arrangement; EFSM – Eurasian Fund for Stabilization and Development; NAFA – North American Framework Agreement; ESM – European Stability Mechanism; EFSM – European Financial Stabilization Mechanism; EU BOP – EU Balance of Payments Assistance; EU MFA – EU Macro Financial Assistance.⁵ Note that Hong Kong and Palestine are included here as RFA member countries but not as IMF member countries.

* Total resources stated by the IMF is SDR 978bn; lending capacity is stated to be SDR 715bn (about USD 958.1bn) (IMF n.d.a). Authors' data sum up to USD 927bn based on member country's quota under normal access (maturity of one year of 145% of paid in quota).

** Estimated volume for 2018, based on Denbee et al. (2016), updated by Essers/Vincent (2017). We follow Denbee et al. (2016) by assuming that the reciprocal nature of currency swaps among advanced economies requires counting each swap twice, and by assuming that the unlimited swap lines between the US Fed and the ECB, Canada, Japan, United Kingdom, and Switzerland can be estimated by the amounts drawn during the global financial crisis, which sums up to about USD 600bn. When we apply these assumptions to our estimates for the year 2018, the amount of total active swaps sums up to about least USD 1.5tr.

*** As to our knowledge, no systematized overview on short term lending of multilateral development banks exists. Yet, several have established credit lines for emergency lending during the global financial crisis, such as the Asian Development Bank Countercyclical Support Facility or the Interamerican Development Bank's Special Development Lending. In response to the COVID-19 pandemic, again, multilateral development banks announced temporary short-term liquidity access between USD 1bn (European Bank for Reconstruction and Development), USD 6.5bn (Asian Development Bank) and USD 8bn emergency finance by the International Finance Corporation under World Bank's COVID-19 lending of about USD 160bn (<https://www.worldbank.org/en/news/feature/2020/04/02/the-world-bank-group-moves-quickly-to-help-countries-respond-to-covid-19>).

FIGURE 2

Source: Authors' compilation based on World Development Indicators 2020, IMF (n.d.a.), RFA websites and annual reports and Denbee et al. (2016) updated by Essers/Vincent (2017). Notes: According to World Bank classification of regions, East Asia & Pacific includes: Australia, Brunei, Cambodia, China, Hong Kong, Fiji, Republic of Indonesia, Japan, Kiribati, Korea, Lao, Malaysia, Marshall Islands, Micronesia, Mongolia, Myanmar, Nauru, New Zealand, Palau, Papua New Guinea, Philippines, Samoa, Singapore, Solomon Islands, Thailand, Timor-Leste, Tonga, Tuvalu, Vanatu, Vietnam; Europe & Central Asia includes: Albania, Armenia, Austria, Azerbaijan, Belarus, Belgium, Bosnia, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Georgia, Germany, Greece, Hungary, Iceland, Ireland, Italy, Kazakhstan, Kosovo, Kyrgyz Republic, Latvia, Lithuania, Luxembourg, Moldova, Montenegro, Netherlands, North Macedonia, Norway, Poland, Portugal, Romania, Russian Federation, San Marino, Serbia, Slovak Republic,

⁵ Lending capacity per country of regional funds is calculated for one year based on the information given on their websites or in annual reports. ESM, EFSM, EU BOP and EU MFA lending capacity per country is estimated by relative GDP shares as maximum drawable amount of the total available lendable volume. The figures for CRA and CMIM include the total amount of accessible liquidity, including the 70 percent that are only available upon agreement on an IMF program.

Slovenia, Spain, Sweden, Switzerland, Tajikistan, Turkey, Turkmenistan, Ukraine, United Kingdom, Uzbekistan; South Asia includes: Isl. Rep. Of Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, Sri Lanka; Sub-Saharan Africa includes Angola, Benin, Botswana, Burkina Faso, Burundi, Cabo Verde, Cameroon, Central African Republic, Chad, Comoros, Congo Democratic Republic, Cote d'Ivoire, Equatorial Guinea, Eritrea, Eswatini, Ethiopia, Gabon, Gambia, Ghana, Guinea, Guinea-Bissau, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mauritius, Mozambique, Namibia, Niger, Nigeria, Rwanda, Sao Tome & Principe, Senegal, Seychelles, Sierra Leone, Somalia, South Africa, South Sudan Republic, Sudan, Tanzania, Togo, Uganda, Zambia, Zimbabwe; Latin America & Caribbean includes Antigua and Barbuda, Argentina, Bahamas, The Barbados, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominica, Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Suriname, Trinidad and Tobago, Uruguay, Venezuela; North America includes Canada and USA; Middle East & North Africa includes Algeria, Bahrain, Djibouti, Egypt, Iran, Iraq, Israel, Jordan, Kuwait, Lebanon, Libya, Malta, Morocco, Oman, Palestine, Qatar, Saudi Arabia, Syrian Arab Republic, Tunisia, UAE, Yemen.

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GLOBAL ECONOMIC GOVERNANCE INITIATIVE

The Global Economic Governance Initiative (GEGI) is a research initiative at Boston University's Global Development Policy Center. The GDP Center is a University wide center in partnership with the Frederick S. Pardee School for Global Studies. The Center's mission is to advance policy-oriented research for financial stability, human wellbeing, and environmental sustainability.

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