

**IEO** Independent Evaluation Office of the International Monetary Fund  
مِنْتَدَى الأَقْصَادِيينَ العربِ  
1866 **AUB** American University of Beirut الجامعة الأمريكية في بيروت

Le Cercle des Economistes Arabes  
And the Independent Evaluation Office (IEO) of the International Monetary Fund

In partnership with  
Applied Economics and Development Research Group  
American University of Beirut (AUB-AED) and Banque BEMO

**The IMF and Fragile States**  
Evaluation Report 2018  
Presentation & discussions

**BANQUE BEMO**

Beirut, July 31 2018  
Michel and Sherine Bayoud Lecture Hall  
American University of Beirut, Faculty of Agricultural and Food Sciences (FAFS)

Tags  
#arab\_fragile\_states  
#arab\_economists\_and\_aub

## Minutes of Beirut workshop of July 31, 2018

The *Cercle des Economistes Arabes* and the *Independent Evaluation Office* (IEO) of the *International Monetary Fund* (IMF) had jointly organized, in partnership with the *Applied Economics and Development Research Group* at the *American University of Beirut* (AUB-AED) and Banque BEMO a workshop in Beirut on July 31, 2018 for the launching and discussion of the 2018 evaluation report of the IEO: the IMF and the Fragile States (FCS). The workshop involved 15 discussants and around 100 participants from the finance, banking and research community.

Since the introduction, it was pointed out that many Arab countries present today different criteria of fragility: not having stable governments or in a conflict or turbulent transition, weak institutions and large corruption, not closing properly their budgets, vulnerable to shocks, including that of the “Arab Spring”, humanitarian crisis, intervention of foreign countries and troops, etc. This is while many of these countries were founding members of the IMF at the Bretton Woods conference, precisely to insure “macroeconomic stability” following independence. The question is then raised on how the IMF could help retrieving financial stability, especially for the post-conflict countries.

In this context, the IEO was created in 2001, just after the Asian financial crisis, to analyse the relevance and efficiency of IMF policies, trying to help restoring credibility of and public faith in the IMF. It aims at informing the executive board in its oversight on IMF activities, assisting staff and management to learn from experience and to strengthen external credibility. The IEO had already produced 27 reports which had shown its independence from management and had seen a follow-up process to improve and implement recommendations. The choice of making a report on “Fragile States” is justified by the significant needs of the concerned countries and by the spill-over risks, owing that in these cases the IMF cannot do “business as usual”.

The IEO evaluation report points that the Fragile States pose major challenge for IMF standard business model, as there is poor governance, low absorptive capacity and exposure to security

shocks. It is one of the most urgent global issues. Also, there is no formal definition of which an FCS is. The internal approach of the IMF identifies 39 States as such. Their list is not published. Most are concentrated in the Middle East and Africa. The report did not analyse them all but focused on only 24. While a 2012 guidance note to the staff recognized their special characteristics, there is no dedicated lending facility to the FCS. The main impact of IMF involvement had been through technical assistance to help build core policy institutions and to catalyse donor support. However, the discrepancy between the short-term focus of the IMF and the long-term needs of FCS was depicted, as well as the low program completion at only 27%, the concentration of technical assistance in a handful of countries and the little difference in conditionalities between FCS and non-FCS. All these generated tensions. The IMF faced also other issues such as little institutional collaboration with other development partners, high risk averse and lack of field experience, high staff turnover and inadequate allocation of staff resources on FCS. The report concludes that *“the IMF’s approach to FCS seems conflicted. It has not consistently made the hard choices needed to achieve full impact; past efforts have not been sufficiently bold or adequately sustained; staff has tended to revert to treating fragile states using IMF-wide norms, rather than as countries needing special attention”*. The report notes also that these shortcomings persisted *“because the institution has not developed a full consensus”* while there is a need to adopt *“meaningful adjustments to its approaches on a bolder and more sustained basis”*. It recommended adapting a lending tool kit for FCS needs, practical steps to increase impact of capacity development, strengthening staff incentives to such work, to issue a high-level commitment with specific institutional mechanisms and country strategies toward FCS.

The first session focused on “dealing with fragility” particularly for the case of Iraq and was moderated by the 2<sup>nd</sup> Vice-Governor of Lebanon Central Bank. The differences in definition of fragility between the IMF and the World Bank (WB) were depicted, as well as how fragility is distinguished from failure and linked to war. In such a situation, governments have short term sights, on how to pay civil servants, insure minimum services and create stability, while underground the social contract is being eroded. Examples from Afghanistan and Georgia were addressed. The main concern is then to build or rebuild institutions, while there is low absorption capacity and strong and destabilizing vested interests; and this is a long step by step process which cannot generate leapfrog “big gains” to the population.

The financial needs could be important in some cases. This is while the IMF intervene on short term and is not the cheapest source of budget support concessional financing, having strict conditionalities on social spending. Iraq obtained a standby arrangement from the IMF in 2016 but its importance lays in triggering other donors support with much larger amounts. This came following the large drop of oil prices in 2014 while crude oil represents almost the unique source of revenue and exports for Iraq. And precisely, this non-diversification of the resources is a main reason of fragility for Iraq.

During the public discussion, questions were raised on why the IMF and the donors had not enable Iraq to extract itself from its “fragile” situation after 15 years of support or Palestine to build an independent institutional macroeconomic framework? Also, the questions interrogated on how the ambiguities of the definition of a “fragile state” are used for pressuring some governments?

The recommendations of the IEO report had been further presented, noting that the IMF is conflicted, not enabled to deliver what it should deliver as “a contribution to global public good” but willing to change its normal practices and procedures for the cases of “fragile states”. The reviews did not lead to the bold initiatives needed. IEO’s recommendations follow the intuitions that IMF staff had on how to work for these cases and tried to find the institutional ways to bring the profound change needed, especially concerning a deeper IMF commitment. 6 recommendations

addressed the issue that too many IMF programs went off track as the “hurdle for FCS was set too high” and that there is a need to insure a transition between the emergency “rapid financing” available for countries in conflict to the upper credit tranche and to provide better focused assistance. Also, it was recommended that the executive board and the IMFC to endorse a stronger IMF role towards FCS, that a high-level committee be formed for that purpose and that comprehensive country strategies be elaborated. These recommendations were discussed by IMF’ executive board last March 22 and the need for change acknowledged. An implementation plan is due in September.

The second session targeted generally the issues of financial stability and the IMF. The discussants, including former IMF staff, considered the IEO report as a step forward, but is still a shy attempt to assess the issue and need to be much bolder. A “cultural revolution” is needed at the IMF. The staff working on FCSs has significantly more impact and added-value than those dealing with developed economies. Also, there is no IMF department dealing with the institutional build-up which is a much more important target in FCS than the macroeconomic framework. They noted that Lebanon could qualify as an FCS with the criteria of the presence of a UN peacekeeping force or others as well. They noted also that the IMF has been reluctant to lend to countries that have uncertain capacities to service their debts while these are precisely the countries in need and foreign aid to developing countries had considerably diminished in the last decade. They also depicted that IMF article IV recommendations are uniquely focused on increasing taxes and lifting subsidies, with little focus on increasing the size of the economy and dealing with the informal one. And typically, the informal part of the economy is significantly large in FCSs and the tax evasion and exemptions are very large. Concerning the high turnover of IMF staff, the joke was made that local stakeholders conduct a “reverse technical assistance” towards the staff to learn about the complexities of their countries. Otherwise, the discussants criticized how the IMF strongly pushes FCS to establish capital and stock markets, while these markets would face shallowness, illiquidity, manipulated and susceptible to shocks. Even countries like Lebanon and Turkey with more developed markets face major difficulties with international market access. Devaluation of their currencies or significant increase of their interest rates destabilize their economies.

IEO representatives agreed with most of these comments. However, they informed that the aid agencies did not encourage the IMF to be itself a “development finance institution”, what constitutes a constraint for the action and resources of the IMF. Also, the issue of balancing between macroeconomic stability and growth is not easy.

The public discussion of this session raised the question of contradictory priorities and recommendations for FCS between the IMF and other donors, including the World Bank. And this creates confusion and impede efficiency. Otherwise, it was noted that FCS are often divided or led by repressive junta or non-fully recognized governments at the international level, so the question is made on how the IMF can deal with the different actors involved, sometimes non-state. The immediate example for that is Libya where there are in practice two governments and two central banks. There is an issue in the political economy of the IMF. Why some countries are rewarded and other sanctioned while both have repressive regimes? Why the IMF buys the government discourse and policy in his article IV consultations, like in Lebanon, on raising taxes while it “turned a blind eye” to the demands for stopping wasteful spending? Why the IMF does not talk with other stakeholders than the government, like other donor agencies, with the risk of losing legitimacy? Otherwise, some economic powers have a control voices within IMF board and dictate their policies on some countries through the IMF. And the IMF is not held accountable of its imposed policies on countries in need, while it does not consider all the aspects of their economic “tissues” and is impacting and catalyzing other agencies to deliver aid. What happens when austerity policies

imposed by the IMF contradict necessary development and economy broadening policies? There is an “elephant in the room”.

The IEO answered that the IMF is not specialized in development policies, but recommendation 2 of the report suggested the creation of departmental committee chaired by a senior staff or an FCS unit. Ultimately the board of the IMF has to decide how best to address FCS situations and the issues identified. The IEO recognized that there is an “elephant in the room” on governance issues, but the “elephant looks different in each country”.

The last session was put under the title of “the way forward”. The discussants pointed that the IEO report noted that Fragile States were disadvantaged, comparatively to other states, both in terms of financial assistance (and non-completion of programs) and technical assistance. All the obstacles mentioned for fragile states precisely define fragile states... And, finally the report says that IMF cannot be efficient in fragile states because they are fragile states! ... And as the report points that macroeconomic stability cannot solve the governance and development issues, it indicates clearly that dealing with fragile states cannot be addressed without widening the scope and mandate of the IMF. The evident example is that raising taxes cannot be a solution if corruption is very large and public trust in government very low. Good institutions and trust in them are essential for macroeconomic stability. In the case of Lebanon, the announcements of the “Cedar Conference” didn’t have their economic effects as Lebanese had lost trust in their government. Otherwise, the discussants noted a quotation of the report that *“the outcome of any IMF intervention is critically influenced by political, military, and security decisions including by international actors outside the Fund’s control”*. The situation of FCS is not only the consequence of internal dynamics, but often also of colonization and extraction of resources by foreign powers and companies. In most cases, their conflicts are proxy wars. The G7 countries represent 45% of the voting powers at the IMF while they are responsible of most of the wars in the region and are the weapons sellers. So, what is the nature of leadership required from the IMF? And can its political role and responsibilities be considered outside the peace building of the UN and the Security Council? The typical cases are Libya and Syria. Also, the discussants recommended that the IMF involve professionals from the FCS leaving abroad in the institutional capacity building to have best results, as some UN agencies. A program for qualifying young professionals from FCS should also be supported by the IMF. Discussants argued that Lebanon, where this workshop is held, is one of the least fragile states in the world and can probably help the international community. The concept of “anti-fragility”, as invented and popularized by Mr. Nassim Taleb the author of the “Black Swan”, was introduced. “Anti-fragile” states may benefit from stress. In the last 50 countries, Lebanon had a civil war, 3% of its population as casualties, 1/3 of its population took refuge outside, few years later it managed to host refugees coming from Syria and Palestine representing a quarter of its population, its currency lost more than 99% of its value, it had and have several foreign armies on its soil, its state is dislocated not offering basic public services. Despite all that, this nation has prospered more than its neighbors and is today more powerful than before its civil war. Lebanon is a paragon of anti-fragility. But this anti-fragility should be by design and not by accident. Lebanon needs to improve anti-fragility and give it purpose at the international level. But this concept was argued, as Lebanon had lost the opportunity for a much better growth, mainly because of imbedded corruption and weak state. Finally, the discussants questioned on how the IMF shall react to this report and evolve, as the experiences of the Latin American, Asian and other crises did not lead to major changes within the IMF and its approaches, despite their severity. Skepticism is raised on the possibility of such evolution. The IMF addresses its critics always towards weak or fragile states, and never on G20 countries, even if their policies have a huge impact on the globalized economy. Maybe the need for change is more essential today as USA itself is changing the global rules of the economic game that had based IMF policies for long. This is while the countries that refused IMF recommendations are those who have succeeded. They relied on themselves.

The public discussion insisted on the necessity to assess situations beyond the GDP and national accounts. It also pointed that the role of the IMF is highly political. This is while no clear and precise rules governing this role and how it respects sovereignty of the countries. There is also many methodological details needing further discussions with the IMF, as per dealing with “total social contributions” instead of only taxation and per assessing accounts on the national and regional levels.

Finally, the IEO and all participants concluded that helping fragile states is a global public good and a priority, and this need joint efforts.

### ***The program***

# **The IMF and Fragile States**

**Evaluation Report 2018**

**Tuesday July 31, 2018 | 3:00 – 7:00 pm**

**at the Michel and Sherine Bayoud Lecture Hall**

**American University of Beirut, Faculty of Agricultural and Food Sciences (FAFS)**

**2:30- 3:00 Registration of participants**

**3:00-3:10 Welcoming: Samir Aita, President of the Cercle des Economistes Arabes and Mr. Charles Collyns, Director of the IEO/IMF**

**3:10-3:40 Main Findings of the report, Mr. Shinji Takagi, Assistant Director IEO**

**3:40-4:30 1<sup>st</sup> Session: Dealing with Fragility. Moderator: Dr. Saad Andary, 2<sup>nd</sup> Vice Governor, Banque du Liban. Panelists: Dr. Saladin Hadeethi, Director of Debt, Iraq Ministry of Finance, Dr. Sahar Najeedee, Director of Statistics, Central Bank of Iraq; Mr. Robert Tchaidze, Senior Economist in the Middle East and Central Asia Department of the IMF. Followed by debate with audience.**

**4:30-4:45 Coffee Break**

**4:45-4:55 Recommendations of the report, Mr. Charles Collyns**

**4:55-5:55 2<sup>nd</sup> Session: Financial stability and the IMF. Moderator: Dr. Jad Chaaban, AUB and Cercle des Economistes Arabes. Panelists: Mr. Nassib Ghobril, Chief Economist Byblos Bank Group; Dr. Mazen Soueid, Chief Economist Bankmed; Mr. Karim Daher, President of the Lebanese Association for Taxpayers' Rights (ALDIC). Followed by debate with audience.**

**5:55-6:45 3<sup>rd</sup> Session: The Way Forward. Moderator: Mr. Samir Aita. Panelists: Dr. Youssef Al Khalil, Banque du Liban; Dr. Talal Salman, UNDP, advisor to the Minister finance, Lebanon; Dr. Riad Obegi, President Banque BEMO; Dr. Irma Majdalani, former Dean of the Faculty of Economics, University of Saint Joseph, Lebanon. Followed by debate with audience.**

**6:45-7:00 Closing: Charles Collyns and Samir Aita**

**7:00-8:00 Cocktail**