AFRICATALYST

GUIDANCE NOTE ON THE IMF RESILIENCE AND SUSTAINABILITY FACILITY

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Executive Summary

The Resilience and Sustainability Facility (RSF) is a lending instrument of the IMF created under the Resilience and Sustainability Trust (RST) which was established in April 2022 to help low-income, vulnerable middle-income countries and small island states address longer-term structural challenges, including climate change and pandemic preparedness. RST resources originate from the voluntary contributions by IMF members with strong external positions who have channeled part of their reserve assets including SDRs to support eligible countries.

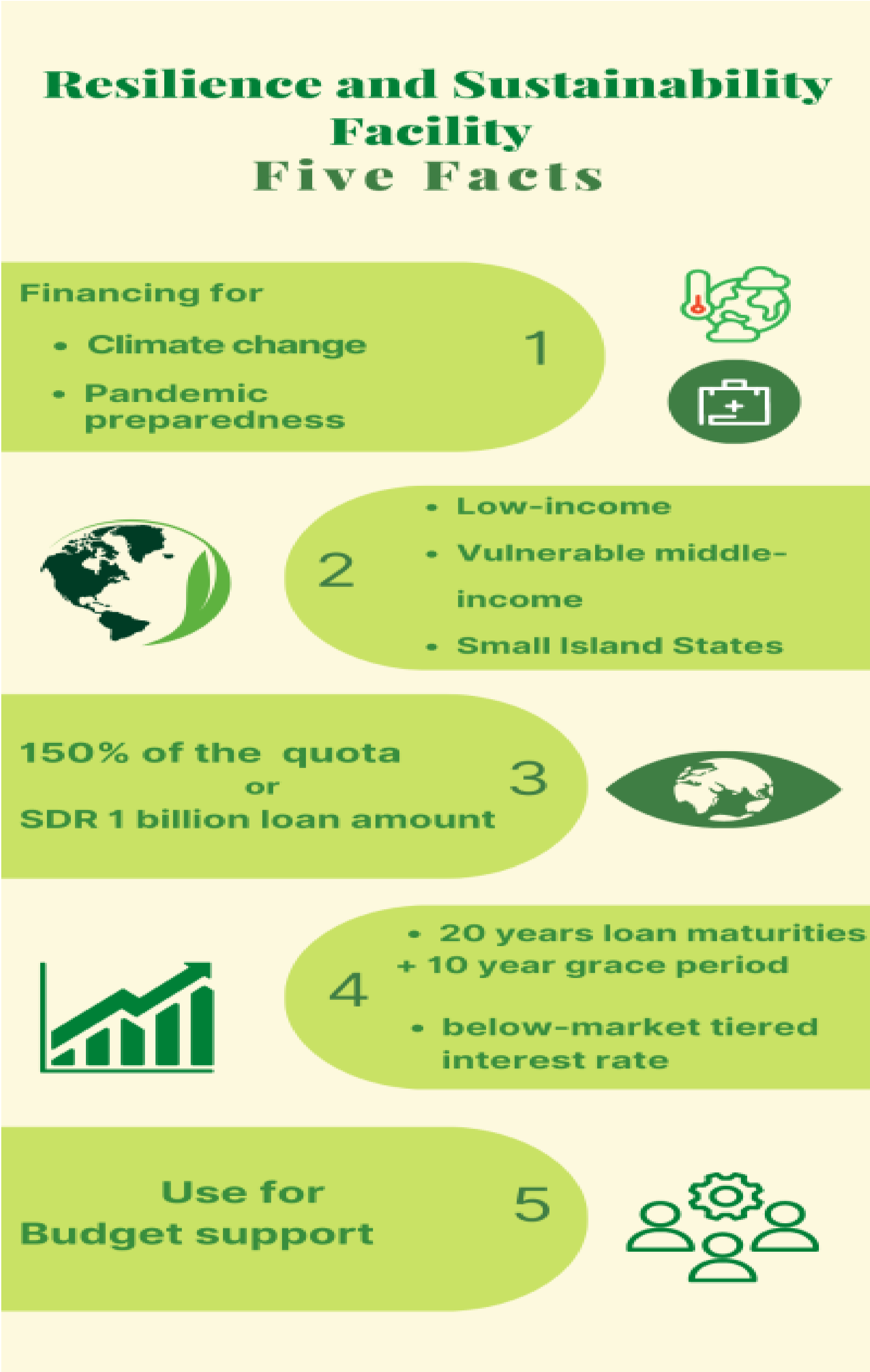
The RSF is designed to help countries address immediate financing needs through budget support to implement climate-resilient initiatives such as green infrastructure investments or tax or regulatory policy reforms. Under RSF arrangements, the IMF can provide financing of up to 150 percent of the quota with a maximum of SDR 1 billion per country. Compared to traditional IMF lending facilities, financing under the RSF has a longer maturity of 20 years with a grace period of 10 years.

In addition to the implementation of reforms that build resilience and sustainability and the existence of a current IMF program, access to the RSF is subject to several conditions normally applicable to IMF engagement, including domestic ownership of reforms, consideration of country-specific circumstances, and effective coordination with other multilateral institutions.

To qualify, countries need to have a package of high-quality policy measures aligned with the purpose of the RSF, a sustainable debt level, and adequate capacity to repay the Fund. In collaboration with the World Bank and other regional development institutions with subject matter expertise in climate change and/or pandemic responses, the IMF draws policy priorities from the diagnostics of various tools such as the Climate Change Policy Assessments, the Climate-Public Investment Management Assessment, or the Country Climate Development Reports. The final policy priorities are defined jointly or by the authorities with the support of the IMF based on the tools at its disposal.

The RSF can assist countries in integrating risks related to climate change and pandemics into economic decision-making. Given the significant financing needs of eligible countries, the objective of the RSF is to play a catalytic role in mobilizing complementary funding for climate-related investments, including public and private partnerships.

Key Features of the Resilience and Sustainability Facility



1. Introduction

The COVID-19 pandemic and the increased urgency to tackle the effects of climate change have led the international community to help vulnerable countries address these challenges. Low-income, vulnerable middle-income countries and small island developing States (SIDS) face high adaptation needs whilst contributing little to global warming.[2] For example, the investment needed to build resilience and sustainability are estimated to exceed 5 percent of the GDP in developing countries[3]. For small island countries, these needs could exceed 10 percent of GDP.

As part of efforts to support vulnerable countries, the Executive Board of the International Monetary Fund (IMF) approved in April 2022 the establishment of the Resilience and Sustainability Trust (RST) which is funded from voluntary contributions by IMF members with strong external positions, including through the reallocation of excess Special Drawing Rights. Under the RST, the IMF has established the RSF , a new financing instrument aimed at assisting low-income and vulnerable middle-income countries and SIDS in addressing long-term structural challenges, including climate change adaptation and mitigation, and pandemics.

The RSF aims to support the efforts of national authorities to be better prepared for future pandemics, sustain a low carbon growth rate, and achieve climate-resilient development outcomes. It provides long-term concessional financing to eligible IMF members, which can support domestic budgets in funding investments and policy reforms that build resilience to such shocks, integrate climate and pandemic considerations into decision-making, and facilitate the transition to a more sustainable future, including green public infrastructure.

This guidance note seeks to inform policymakers, the private sector, and civil society in sub-Saharan Africa about the characteristics of this new and innovative lending instrument of the IMF. It discusses the RSF's main features, eligibility criteria, and its role within the broader fabric of international financial assistance. It explores how the RSF could help policymakers as they contemplate various financing options when designing national macroeconomic policies to integrate climate and pandemic risks and the cost of adaptation into their macro-fiscal frameworks. Recent research shows that low-income, vulnerable middle-income countries and SIDS face high adaptation needs.

[2] See Aligishiev, Massetti, and Bellon (2022)

[3] *World Bank Group. CCDR-Synthesis Report (2022)*

2. Overview of the Resilience and Sustainable Trust (RST) and the RSF

RSF loans to eligible IMF members are financed by the Resilience and Sustainability Trust (RST), a new IMF trust account dedicated to promoting climate sustainability in low-income, vulnerable middle-income, and small island developing countries. It complements the IMF's General Resource Account (GRA) and the Poverty Reduction and Growth Trust (PRGT).

The RST is funded by voluntary donations of SDRs by IMF members with strong external positions, particularly advanced economies that do not need to use all their allocated SDRs.[4] In response to the COVID-19 pandemic, the IMF issued USD 650 billion worth of SDRs[5] in a general allocation to its members in 2021. This SDR issuance provided member countries with additional liquidity to deal not only with short-term challenges related to the pandemic and its associated economic crisis, such as buying vaccines and fostering the stability of the global economy but also to address longer-term challenges arising from climate change.

With only the equivalent of USD 21 billion of the allocation going to low-income countries, the RST was created to allow countries with healthy balance of payments positions to channel part of their unused SDRs to help these countries and other vulnerable ones deal with climate change challenges as well as the COVID-19 pandemic.[6] On October 12, 2022, six countries initially contributed USD 20 billion to the launch of the RST, with an additional USD37 billion pledged by thirteen countries.[7] As of December 15, 2022, the total amount of final contributions is of USD 26 billion from eight countries, with France and Korea adding to the list.

Climate resilience building is a macro-critical issue that requires a medium to longer-term perspective. The RSF aims "to support countries in building resilience to structural challenges—such as climate change and pandemics—to help maintain long-term economic and financial stability while catalyzing other public and private financings." IMF members can access RSF financing to increase their policy space and financial buffers to address actual, protracted, or prospective Balance of Payments (BoP) needs due to climate or pandemic impacts or risks.

Figure 1 shows examples of adaptation costs to current and future risks. Coastal protection against rising sea levels can cost small development states 2 percent of GDP annually. Strengthening existing assets and engaging new infrastructure resilience to current storm and flood risks can cost Low-Income countries a total of 1 percent of GDP.

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[4] See Sembene and Mansoor (2022).

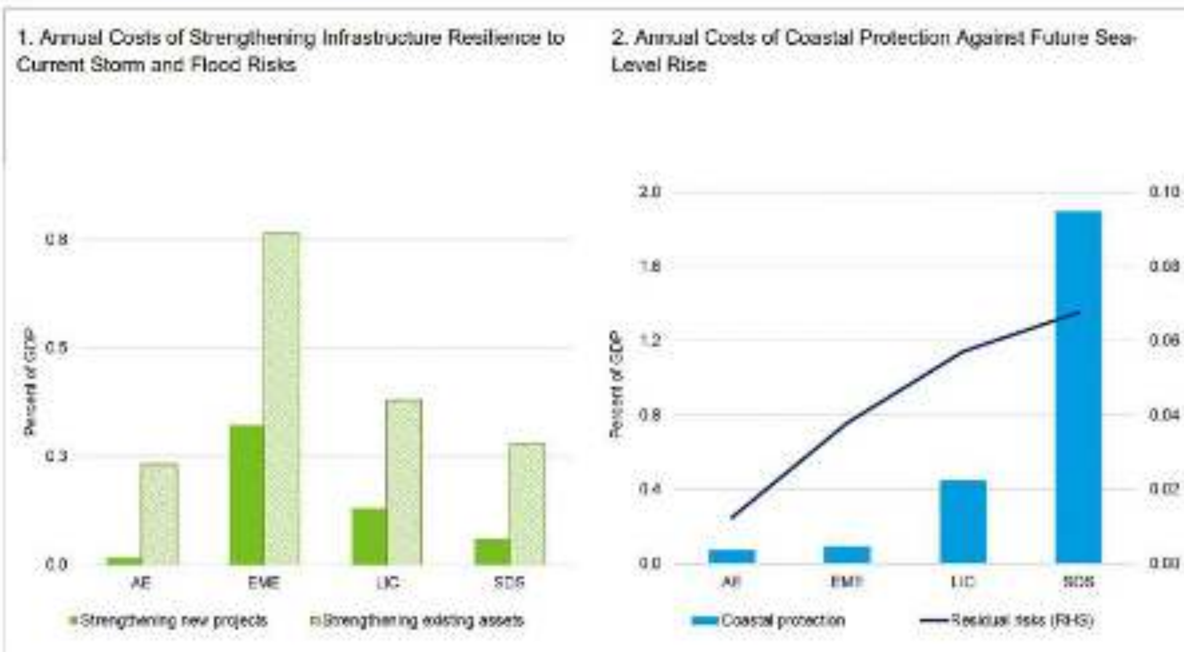
[5] IMF (2021)

[6] The RST pools these resources instead of bilateral arrangements where an individual country lender would need to match with an individual borrower.

[7] Australia, Canada, China, Germany, Japan, and Spain.

The RSF provides lending with loan maturities of 20 years to better align with the longer-term nature of the climate and pandemic challenges. It is the first financing tool of the IMF that provides "long-term" financing at low-interest rates to vulnerable middle-income countries and SIDS. The repayment schedule of each disbursement in 20 semiannual installments starting 10 ½ years after the disbursement.

Figure 1: Public Sector Adaptation Costs to Selected Current and Future Climate Risk



[8]

Source: Hallegatte, Rentschler, and Rozenberg (2019); Rozenberg and Fay (2019); Nicholls and others (2019); IMF, Capital Stock 2019 Dataset; IMF, World Economic Outlook database

Notes: AE = advanced economies; EME = emerging market economies; LIC = low-income countries; SDS = small developing states.

[8] Figure 1 is from: Aligishiev, Zamid, Emanuele Massetti, and Matthieu Bellon (2022). Macro-Fiscal Implications of Adaptation to Climate Change. IMF Staff Climate Note 2022/002. Retrieved on January 01, 2023, from: https://www.imf.org/en/Publications/staff-climate-notes/Issues/2022/03/16/Macro-Fiscal-Implications-of-Adaptation-to-Climate-Change-512769

3. Modalities of RSF Financing

The maximum cumulative access under the RSF for eligible members is determined by the lower of two amounts: 150% of the member's quota or SDR 1 billion (approximately 1.4 billion USD).

RSF loans have a more extended repayment period than traditional IMF loans, with a maximum maturity of 20 years and a grace period of 10 years. Repayment can be in 20 semiannual installments, starting ten and a half years after each disbursement.

RSF disbursements would provide general budget support to address a range of BoP needs including:

- short-term BoP or fiscal needs directly related to implementing reforms to address climate change or the pandemic.
- Increasing policy space for fiscal spending and reforms related to longer-term structural challenges.
- Enhancing longer-term buffers to strengthen a member's ability to withstand shocks related to climate change or other structural challenges.[9]

The RSF is expected to be used for actual borrowing rather than on a precautionary basis. Available financing is expected to be drawn promptly after the IMF Board approves an RSF disbursement.

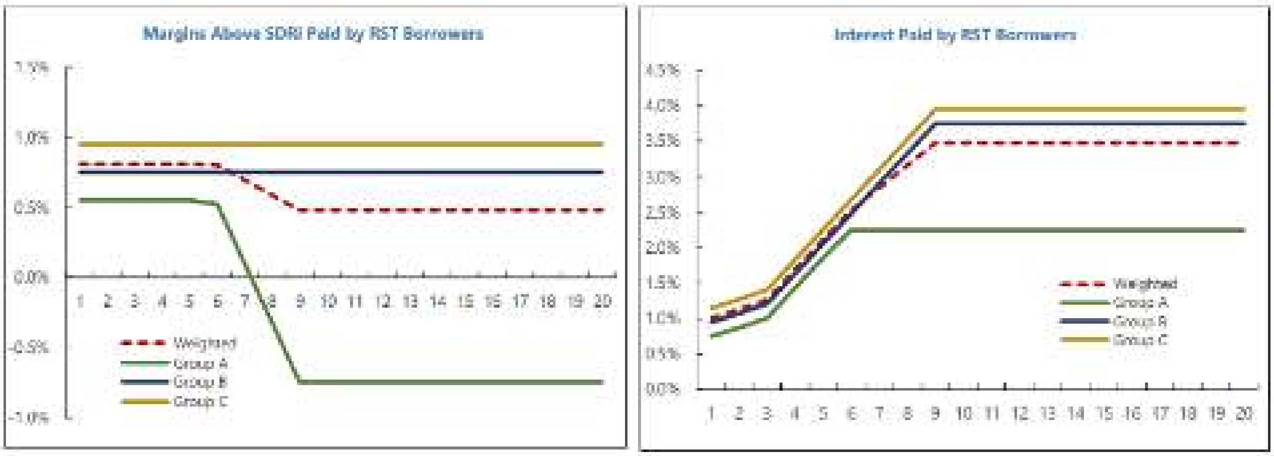
Under the RSF, borrowing countries are charged a tiered interest rate that offers the highest concessionality to the poorest member countries. Group A countries with the lowest incomes pay an interest rate based on the SDR interest rate plus an additional 55 basis points, with no service charge. Group B countries pay an interest rate based on the SDR plus 100 basis points, while the rest of the countries pay an interest rate based on the SDR plus 145 basis points (see Table 1 and Figure 2).

Table 1. Tiered interest rate structure for RSF borrowing

Group	Description	Interest Rate	Service Charge
A	PRGT-eligible countries (51) that are not "presumed blenders"	SDRi + 55 basis points	Exempt
B	"Presumed blenders" of PRGT and GRA resources and all small states with per capita GNI below the cutoff (27)	SDRi + 75 basis points	25 basis points
C	All other RST-eligible countries (including small states with high per capita GNI)	SDRi + 95 basis points	50 basis points

[9] Specific projects could then be financed by the national budget.

Figure 2. Interest Rates Paid by Resilience and Sustainability Trust Borrowers Under Tiered Rates



1 The horizontal axis indicates years of RST operations. The SDRi interest rate is assumed to rise then stabilize at 3% from year 2030. Group A includes PRGT-eligible countries that are not presumed blenders; group B includes presumed blenders and small states with GNI per capita below 10 times the IDA threshold; group C includes all other eligible members that are not included in groups A or B.

Source: International Monetary Fund (2022) Proposal to Establish A Resilience and Sustainability Trust.

The design of the RSF includes safeguards in the form of modest access caps, rules for determining access that specifically considers debt vulnerabilities, enhanced debt structure analysis, debt sustainability, and capacity to repay. These safeguards are designed to provide additional protection for using resources from the RSF due to the longer terms and concessionality under the Facility compared with access under the General Resources Account and Poverty Reduction and Growth Trust.

The duration of an RSF arrangement is 18 months or until all disbursements have been made or upon cancellation or end of the concurrent IMF-supported program. The disbursement schedule of the RSF is contingent on the conclusion of relevant reviews of the concurrent program and distributed equally across the implementation of reform measures agreed upon as part of the RSF arrangement.

4. Eligibility Criteria

4.1. General Qualification Conditions

The RSF is available to approximately three-quarters of the total membership of the IMF based on their income level, market access, and status as small states. Eligible countries include:

(i) low-income countries eligible for IMF financing under the PRGT,

(ii) small states as defined by the IMF, that are IMF members with a population of less than 1.5 million and a gross national income per capita of less than USD 30,000 and

(iii) middle-income countries with a per capita income below USD 12,000 that are vulnerable to financial risks.

4.2. Policy Requirements

In addition to the income and size requirements, countries must meet the following policy safeguards to qualify for RSF loans:

- First, countries must establish a strong foundation for economic stability through high-quality policy measures.
- Second, the country must have a concurrent IMF-supported program with[10] or without financing. Under such a concurrent program[11], authorities need to have the commitment and capacity to implement a set of policies that is adequate to correct external imbalances and enable repayment to the Fund within the specified maturity period.
- Thirdly, each country must have a sustainable debt position and the ability to repay the Fund.

4.3. Conditionality

4.3.1. Formal Requirements

The RSF adheres to the fundamental principles of the IMF Guidelines on Conditionality. These principles include national ownership of reforms, customization to each country's specific circumstances, use of a limited number of conditions, explicit specification of requirements, effective coordination with other multilateral institutions, and review by the Executive Board.

[10] Meaning any use of IMF credit above 25 percent of the SDR quota by a country, referred to as the Upper Credit Tranche.

[11] The IMF-supported program can be financing or non-financing and exclude emergency financing facilities. The arrangements for qualification are Extended Credit Facility, Extended Fund Facility, Flexible Credit Line, Precautionary and Liquidity Line, Stand-by Arrangement, Policy Coordination Instrument, or Policy Support Instrument.

Reform measures under an RSF program must be compatible with the concurrent program's goals. The concurrent program usually contains macroeconomic reforms which put countries on a path with the capacity to pay the IMF back. The concurrent program includes projections for RSF financing in its macroeconomic framework and quantitative targets.

Reform measures for the RSF must be implemented within the duration of the RSF arrangement. However, the timing of implementation of the RSF-linked reforms is flexible, as the measures related to the RSF program typically do not directly affect the balance of payment issues addressed under the concurrent program. Disbursements are linked to the implementation of reforms outlined in the RSF-supported program.

4.3.2. Program Design

The nature of policy measures or reforms that need to be put in place by national authorities to access an RSF loan is evolving with practice under the new facility. Typically, based on the findings of a diagnostics and planning exercise, the IMF has been working with countries to identify specific areas for reform and conditionality under the RSF.

The IMF limited expertise on climate and pandemic-related issues could constrain its ability to effectively assess the relevance of pandemic and/or climate-sensitive investments, policy responses, and outcomes. Accordingly, the IMF collaborates with institutions such as the World Bank and regional development banks[12] to inform the design of a customized policy and reform agenda under RSF programs.

The IMF and World Bank have established principles for coordination on RSF operations, particularly regarding climate-related issues. These principles include:

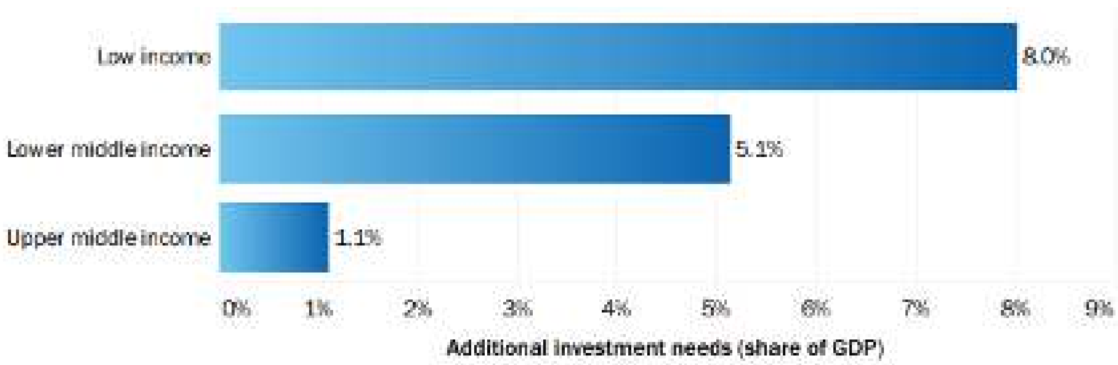
- using diagnostics from both institutions relevant to the RSF's purposes.
- identifying policy priorities for the member country in coordination with the World Bank,
- setting RST conditionality and evaluating whether conditions are met.
- providing a World Bank assessment letter on the country's climate policies and document in the staff report and Memorandum of Economic and Financial Policies that record the country's request for an RSF arrangement, and
- establishing a framework for engagement and information sharing.

The IMF uses various tools to assess a country's climate-related policies, including Climate Change Policy Assessments (CCPAs), Climate Macroeconomic Assessments Programs (CMAPs), green public financial management assessments, Climate Public Investment Management Assessments (C-PIMAs), and assessments of carbon taxation and subsidy reform. The IMF may

[12] In the case of RST lending for pandemic preparedness, the IMF collaborates with the WHO and the World Bank on defining policy priorities.

also consider the policy priorities identified in the World Bank's Country Climate Development

Figure 3: Investment needs for a resilient and low-carbon pathway by income, 2022–30[13]



Reports (CCDRs) when determining the reforms, a borrowing country must implement.

Under the RSF, countries can build reforms to integrate pandemic and climate risks into economic decision-making, prepare for pandemics, adapt to climate change, mitigate the impact of climate change, protect vulnerable populations, develop and implement climate and pandemic finance strategies, build resilience to shocks, improve transparency in climate and pandemic reporting, and assess climate-related and pandemic financial sector risks.

5. Catalytic role and Collaboration Under the RSF

The RSF can help bring public and private partnerships together and catalyze other innovative financing tools. As shown in Figure 3, the investment needs for a resilient pathway between 2022-2030 can reach 8 percent of the GDP for low-income countries. The combined Official Development Assistance (ODA) and Multilateral Development Banks (MDB) lending are less than 10% of what is required to finance the low-carbon transition. However, financial assistance by the IMF can play a role in unlocking other financings, acting as a catalyst for donor financing and leveraging private capital flows.

Effective collaboration among national authorities, the private sector, and the donor community have the potential to amplify the impact of the RSF and deliver on climate and pandemic preparedness financing. For instance, this is critical for bringing down the cost of private finance and crowding in mainstream private capital, notably by removing the risk premium through guarantees, insurance, and blended finance.

[13] Figure 3 summarizes investment needs by income out of the 20 countries from the CCDR-Synthesis Report 2022 of the World Bank. Retrieved on January 01, 2023, from: https://openknowledge.worldbank.org/bitstream/handle/10986/38220/CCDR-SynthesisReport.pdf?sequence=2&isAllowed=y.

According to recent estimates of the leverage ratio of MDBs and public investments, $1 of public investment mobilizes just $0.37 of private investment in low-income countries, $1.06 in lower-middle-income countries, and $0.65 in upper-middle-income countries. [14] The RSF could be an opportunity to advance policies and reforms needed to create new opportunities for private investment and expand MDBs' impact on market development, including local capital markets. For example, the Costa Rican government plans to use RSF-related reforms and its climate agenda to issue environmental, social, and government bonds.

The Rwandan government launched at the COP-27 conference the "Ireme Invest" program, to provide funding for green projects for small and medium enterprises.[15] This is a project worth scaling up. The RSF program's diagnostics can provide information to expand the financing options for countries, including on the natural disaster clause in foreign governments and rating agencies' lending.

Civil society organizations (CSOs) can contribute to the success of an RSF-supported program by collaborating with the government to prioritize projects that benefit the most vulnerable segments of the population. They can help identify needs and develop practical solutions that allow the most vulnerable to adapt to climate change and/or prevent the impact of future pandemics. They can also identify areas that need protection and develop proposals for mobilizing civil society to contribute to building resilience and sustainability through specific interventions.

CSOs also have a crucial role in holding the government accountable for allocating budget resources to priority areas and ensuring that resources are effectively and efficiently used. Development partners active in eligible countries should encourage and facilitate dialogue between CSOs and the government, with a particular emphasis on the role of the private sector.

The authorities can maximize the benefits of the RSF by involving CSOs at an early stage of the dialogue, including keeping the public informed when an application is made. This dialogue could initially focus on identifying shovel-ready projects and project ideas that need feasibility studies. In collaboration with the government, development partners can allocate resources to develop project ideas and implement ready-to-go projects, with the World Bank potentially playing a leading role and the RSF contributing to the necessary counterpart funding. Where the government is slow to act, CSOs can be the catalyst for action by helping develop proposals and, with support from development partners, pressing the government to engage in a dialogue on the implementation and mobilization of additional resources.

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[14] Attridge and Engen (2019)

[1515] The first round of financing for Ireme Invest is $100 million supported by seed funding from organizations such as the Rwanda Green Fund (FONERWA), the Development Bank of Rwanda, and governments from France, Sweden, and the UK, as well as the European Investment Bank and the Green Climate Partnership Fund. Rwanda is also working to develop a green taxonomy to improve the regulatory environment and enable the private sector to make informed green investment decisions. See Ireme https://www.rema.gov.rw/info/details?tx_news_pi1%5Baction%5D=detail&tx_news_pi1%5Bcontroller%5D=News&tx_news_pi1%5Bnews%5D=647&cHash=b443e130bb87e0dfa3dc16aa1aa01f80

6. List of RSF Program Countries (as of January 2023)

<table>
<tr><th>Countries with Staff-level agreements</th><th>RSF amount</th><th>Accompanying Program</th></tr>
<tr><td colspan="3">Barbados</td></tr>
<tr><td></td><td>US$183 million (150% of quota)</td><td>US$110 million (36mo.Extended Fund Facility)</td></tr>
<tr><td colspan="3">“The combined RST and EFF program aims to strike a balance between enhancing resilience to climate change and focusing on Barbados’ continued efforts to reduce public debt and facilitate capital expenditure to boost growth.
Reforms under the RSF include the mainstreaming of climate change in the budget, the introduction of ‘green Public Financial Management’, including in procurement, and measures that would incentivize private sector investments in climate resilient infrastructure and into renewable energy projects.”</td></tr>
<tr><td colspan="3">Costa Rica</td></tr>
<tr><td></td><td>US$710 million (150% of quota)</td><td>US$264 (3rd review of existing Extended Fund Facility of US$1.8bn)</td></tr>
<tr><td colspan="3">“The new facility supports Costa Rica’s pioneering efforts to assess climate risks, decarbonize its economy, strengthen infrastructure resilience, and green the BCCR’s reserves and the financial sector. The RSF will also provide the country with more fiscal space to be able to spend on education and health and other areas”</td></tr>
<tr><td colspan="3">Rwanda</td></tr>
<tr><td></td><td>US$ 319 million (150% of quota)</td><td>36-month Policy Coordination Instrument (PCI)</td></tr>
<tr><td colspan="3">The reforms encompass the following areas:
(i) strengthening and institutionalizing monitoring and reporting of climate-related spending or mainstreaming of climate change in the budget, the introduction of ‘green Public Financial Management,’ including in procurement;
(ii) integrating climate risks into fiscal planning.
(iii) improving the sensitivity of public investment management to climate-related issues;
(iv) strengthening climate risk management for financial institutions;
(v) adoption of measures that would incentivize private sector investments in resilient climate infrastructure and into renewable energy projects; and
(vi) strengthening the disaster risk reduction and management strategy and operations.</td></tr>
<tr><td colspan="3"></td></tr>
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