



IMF Should Use Excess Windfall Profits from Gold Sales to Cancel Debt for Poor Countries in Crisis

Background Paper on a Civil Society Proposal January, 2011

As the International Monetary Fund completes the sale of 403.3 tonnes of gold¹, reaping record profits, the world's poorest countries continue to suffer the aftershocks of multiple crises. The global food, fuel, financial and climate crises all originated in the global North and yet the most vulnerable in the global South disproportionately bear the brunt of these crises. Tens of millions of people have been pushed into extreme poverty and poor country governments been forced to increase their debt burdens through no fault of their own. Meanwhile, traditional development assistance is on the decline as countries in the Global North face budget shortfalls of their own.

The projected profits from IMF gold sales already more than cover the IMF's operational and administrative budget needs. At the same time, nonconcessional lending at the Fund has drastically increased Fund revenues. Therefore, it is only appropriate that the \$2.8 billion in excess windfall profits earned from IMF gold sales be directed to help the world's poorest countries become more resilient to crises without having to continue to mortgage their futures to the IMF.

Background on IMF Gold Sales

Since the IMF has historically drawn its operating and administrative funds from fees and interest rates on its loans, its budget faces pressure when lending is down. Prior to the global financial crisis, many borrowing countries were paying back loans faster than the IMF expected due to concerns over loan conditions and the increased popularity of other lenders. With dramatically shrinking income, the IMF projected growing deficits for its operational expenses.

In 2006, the IMF convened a group of experts, chaired by JPMorgan Chase International Chairman Andrew Crockett, to recommend changes to the institution's income model. The group's January 2007 report laid out a new income model based on selling 403.3 tonnes of IMF gold and investing the profits to earn a steady stream of revenue for the institution's operational budget.² The IMF's Managing Director introduced a formal proposal based on the Crockett Report -- the New Income and Expenditure Framework -- at the Fund's spring meetings in April 2008.³ At the time, the IMF projected that gold sales would earn \$7 billion in profits based on a price of \$850 per ounce.⁴

Gold Sales' Contribution to Interest Relief a Minor Step Forward But Still Debt Creating

The global financial crisis and the rising price of gold dramatically altered the budgetary outlook for the IMF. In April 2009, the G20 designated the IMF as the main responder to the balance of payments crises resulting from the financial crisis, and tripled the Fund's lending capacity from \$250 billion to \$750 billion. At the same time, as the gold sales began in 2009, the price of gold was much higher than expected and continued to climb until all the gold sales were completed on December 21, 2010.

¹ At the end of December 2010, the IMF announced it had sold all 403.3 tonnes of gold, reporting a total of \$14.7 billion in profits. See International Monetary Fund, "IMF Concludes Gold Sales," December 21, 2010, imf.org

² At 3,217 tons, the IMF holds the third largest gold reserve in the world after the United States and Germany.

³ Crockett, Andrew, "Final Report of the Committee to Study Sustainable Long-Term Financing of the IMF," January 31, 2007, imf.org

⁴ Interview with U.S. Treasury officials, January 13, 2010.

In 2009, civil society organizations intensively campaigned for gold sales profits to benefit poor countries, pressing IMF shareholder governments to require that at least \$5 billion in profits from gold sales be directed toward non-debt creating assistance for low-income countries.⁵ In July 2009, the IMF responded by announcing its intent to increase its concessional lending to low-income countries to \$8 billion over two years. As part of the plan, \$900 million in windfall profits from gold sales (defined as profits above the projected \$850 per ounce) would subsidize two years of interest relief on those concessional loans.

This much-heralded assistance to low-income may have reduced interest payments for low-income countries but it did not provide these countries with the non-debt creating assistance that they need. IMF assistance to low income countries still creates new debt, regardless of temporarily low interest rates. Even on the IMF’s own terms, the reduction in interest payments was marginal - an average of less than \$1 million per year for countries that qualified.⁶ Further, the IMF board’s agreement to partially finance the subsidy with \$900 million in gold sales windfall fell far short of civil society’s demands for \$5 billion from gold sales for low-income countries. The short-term interest reductions also required \$600 million in additional contributions from donors’ limited aid budgets.

More than \$2 Billion “Excess” Windfall Profits from Gold Sales, Not Needed by the IMF

When the IMF committed to use a portion of profits from gold sales toward minimal interest relief for low-income countries, they assumed that gold prices would average \$920 per ounce⁷ (over the initial \$850 per ounce projections). As the Fund began on-market sales in February 2010 and gold prices continued to climb, it became clear that there would be even more “excess” windfall profits (above \$950 per ounce). By November 2010, gold prices had reached a high of \$1424 per ounce.⁸ On December 21, 2010, the IMF announced the conclusion of its on-market gold sales, which netted the institution \$10.7 billion in total -- at least \$3.7 billion more in profits than originally projected in 2008. Even after funding the 2009 interest relief subsidy agreement, the Fund will realize \$2.8 billion in excess windfall profits.

IMF Profits from Gold Sales (in U.S. Dollars)	
Profits Realized from Gold Sales completed in December 2010	\$14.7 Billion
Book Value of Gold	- \$4 Billion
Committed for IMF New Income Model in 2008	- \$7 Billion
Committed for LIC interest relief in 2009	- \$900 Million
Uncommitted windfall profits	\$2.8 Billion ⁹

⁵ One example of policy statements by civil society organizations in 2009 is Jubilee USA’s “Leveraging IMF Pots of Gold for Low-Income Countries,” May 15, 2009, jubileeusa.org

⁶ Bretton Woods Project, ActionAid, Third World Network, Eurodad, “IMF Financial Package for Low-Income Countries: Much Ado About Nothing?,” August 7, 2009, brettonwoodsproject.org

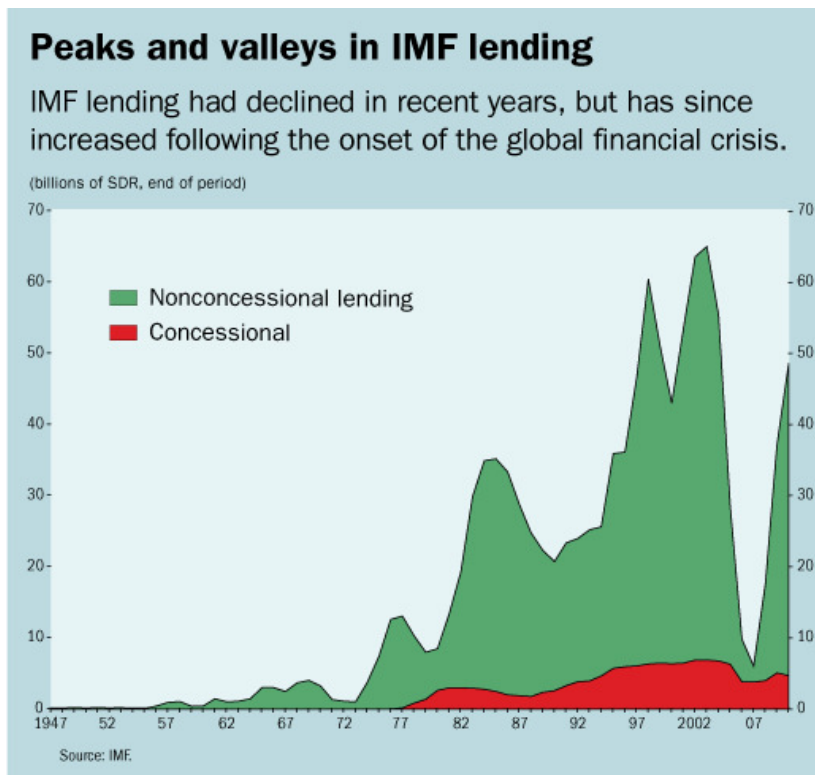
⁷ Interview with U.S. Treasury representatives, January 13, 2010.

⁸ “IMF’s gold sales slowed 40 pct in Oct. vs Sept,” *Reuters*, Nov 30, 2010, reuters.com

⁹ This number is approximate, due to rounding errors, the changing exchange rates for SDRs, and possible “leakage” when funds are passed to member governments before being returned to and distributed by the IMF. Source: Interview with U.S. Treasury officials, January 13, 2010.

The IMF's new income model, approved in 2008, projected that gold sales at \$850 per ounce would net \$7 billion. This invested 3 per cent per year would generate at least \$200 million of extra income annually. Now, that the IMF's lending capacity has tripled (see graph at right), thanks to more than \$500 billion in New Arrangements to Borrow from G20 countries, its income needs from gold sales are much less than when the IMF initially approved them. Hence, the IMF has already more than met its original aim for stable administrative financing, without considering the excess windfall profits from gold sales. While the IMF will propose to refurbish its headquarters in Washington, DC as part of a 2011 workplan, it

would be unconscionable for the Executive Board to prioritize improving the IMF's already opulent DC office buildings over providing non-debt creating finance for the most vulnerable countries.



A Civil Society Proposal: Direct Excess Windfall Profits to Crisis Debt Relief

When countries face external shocks that threaten their vulnerable populations and long-term development, they need debt relief and grant equivalent assistance without harmful conditions. The IMF's newly created Post-Catastrophe Debt Relief Trust Fund provides an initial framework for creating a better mechanism for the IMF provide debt cancellation in times of crisis.

Mounting IMF Debts for Countries in Crisis

The global economic crisis in 2009, which came on the heels of a food and fuel crises in 2008, forced many low-income countries to take on new debt through no fault of their own. The growing climate crisis, which once again originated in the global North, also disproportionately affects the world's poorest countries, and has resulted in new debt as countries borrow to prepare for and recover from climate-related disasters.

In the wake of the global economic crisis, the G20 acknowledged the impact of these crises on poor countries and directed the international financial institutions to create better mechanisms to assist poor countries cope with such exogenous shocks. The World Bank's International Development Association (IDA) created a pilot "Crisis Response Window" which they aim to make permanent.

IDA's Crisis Response Window proposal stated "The succession of a series of global crises and natural disasters has led to an increasing recognition that there is a gap in the international aid architecture to

systematically assist LICs in dealing with the impact of large shocks on government core spending and on the poor and vulnerable.”¹⁰

Unfortunately, nearly all crisis assistance thus far has come in the form of new loans, which threatens long-term debt sustainability. The IMF has been given the role of mobilizing needed finance quickly to governments when exogenous shocks hit. Since the global economic crisis, the IMF has ramped up lending capacity to low-income countries to \$17 billion over the next four years. However, even loans with interest relief for low-income countries amount to new debt that many of the poorest countries cannot afford. A study by the Center for Global Development found that almost half of IMF crisis lending to Heavily Indebted Poor Countries (HIPCs) went to countries already in debt distress or in high risk of debt distress. For example, in the case of the DRC, \$276 million in new post-crisis IMF loans in 2009 will virtually cancel out the \$320 million in debt relief the Fund is set to provide the country once it reaches the HIPC completion point.¹¹ For post-completion point HIPCs facing exogenous shocks that lead to balance of payment crises, there has not been a mechanism for the Fund to provide deeper debt relief or grant equivalent assistance.

The excess windfall in gold sale profits should therefore be directed to fund debt cancellation and/or non-debt creating assistance for poor countries in crisis.

IMF’s Post-Catastrophe Debt Relief Trust Fund

In the days after the catastrophic earthquake devastated already impoverished Haiti, the IMF announced a \$100 million emergency loan to the country. The international advocacy community immediately demanded that all assistance to Haiti be in grant form, and successfully pushed the G7 finance ministers to support that call. The IMF’s Managing Director responded by stating his intention for the Fund to cancel all of Haiti’s debt to the institution including the new loan. In June 2010, the IMF launched the Post-Catastrophe Debt Relief Trust Fund in order to allow the IMF to participate in coordinated international responses to extraordinary catastrophes, such as Haiti. The IMF created the PCDR Trust to provide a two-year moratorium on debt service payments and possible debt stock cancellation to countries that qualify for the World Bank’s most concessional lending from IDA and that face a catastrophic natural disaster, specifically those that have (1) directly affected at least one third of the population and (2) destroyed more than a quarter of the country’s productive capacity or caused damage deemed to exceed 100 percent of GDP.¹²

The PCDR Trust was initially financed by transferring SDR 280 million (equivalent to \$422 million) from internal IMF resources, with the expectation that donors would replenish the trust with future contributions.¹³ On July 21, 2010, the IMF Executive Board agreed to use the PCDR Trust to eliminate all of Haiti’s \$268 million debt stock to the IMF,¹⁴ including the \$100 million emergency loan, which depleted the PCDR Trust Fund to \$154 million. Currently, there are no apparent donor pledges to replenish the Fund.

Expanding from a “Post-Catastrophe” to “Crisis” Debt Relief Fund

¹⁰ International Development Association IDA Resource Mobilization Department, “Proposal for a Pilot IDA Crisis Response Window,” November 23, 2009, worldbank.org

¹¹ Leo, Benjamin, “Will World Bank and IMF Lending Lead to HIPC IV? Debt Deja-Vu All Over Again - Working Paper 193,” Center for Global Development, November 23, 2009, cgdev.org

¹² International Monetary Fund, “The IMF’s Post-Catastrophe Debt Relief Trust,” July 21, 2010, imf.org

¹³ International Monetary Fund, “The IMF’s Post-Catastrophe Debt Relief Trust.”

¹⁴ International Monetary Fund, “The IMF’s Post-Catastrophe Debt Relief Trust.”

The international community welcomed the IMF's cancellation of Haiti's debt, as an important step forward in allowing the Fund to provide needed debt relief to impoverished countries in crisis instead of adding to their debt burdens. However, the eligibility criteria for the PCDR Trust is far too narrow and the financing far too little to allow the Fund to provide needed debt relief to the range of poor countries facing exogenous shocks. At the time the IMF Executive Board approved the Trust Fund, some board members believed the criteria should be less restrictive.¹⁵ Some also noted that, in future, it might be appropriate to use the profits from gold sales to help finance the Trust.¹⁶

Anti-poverty, development, and other civil society organizations strongly urge the IMF Executive Board to expand the eligibility criteria for the Post-Catastrophe Debt Relief Trust Fund so that it is a "Crisis" Debt Relief Trust Fund - available to countries facing severe natural disasters as well as other exogenous shocks.

There is recent precedent for such expanded criteria: the World Bank's International Development Association's Crisis Response Window includes both natural disasters and economic crises resulting from external shocks. The Crisis Response Window, which is to be made permanent in the IDA 16 replenishment, would provide special CRW financing to IDA countries facing natural disasters and other exogenous shocks. A country would become potentially eligible for support through the Crisis Response Window if it faces (1) an economic crisis that affects several IDA countries and is expected to result in a year-on-year GDP growth decline of at least 3 percentage points (2 percentage points has also been considered as a trigger); (2) an exogenous price shock, such as the 2008 spike in food prices, that has a severe adverse impact on the poor and vulnerable; or (3) a severe natural disaster, determined based on parametric data as well as qualitative assessments of the impact of the disaster. The CRW for natural disasters is not triggered by a simple formula, as it would not take into account the very different characteristics of IDA countries with respect to their size, absorptive capacity and ability to mobilize resources for reconstruction.¹⁷

While the CRW may be a place to start to examine possible criteria for an expanded IMF Crisis Debt Relief Trust Fund, other possible criteria and changes to the Trust Fund could include (not a comprehensive list):

- IDA-blend countries
- Countries that suffer a severe natural disaster as assessed by the United Nations Disaster Assessment and Coordination team
- Countries that face an economic crisis that results in a year-on-year GDP growth decline of at least 2 percentage points
- Countries that suffer exogenous price shocks, with a severe adverse impact on the poor and vulnerable, as measured by an accepted human development indicator.
- Post-conflict countries whose infrastructure and productive capacity has been severely destroyed
- Expand the period of automatic debt service moratorium from two to three years (without interest accrual)

¹⁵ International Monetary Fund, "IMF Executive Board Establishes a Post-Catastrophe Debt Relief Trust," July 21, 2010, imf.org

¹⁶ International Monetary Fund, "IMF Executive Board Establishes a Post-Catastrophe Debt Relief Trust."

¹⁷ International Development Association IDA Resource Mobilization Department "Technical Note on the Establishment of a Crisis Response Window in IDA16," September 2010, worldbank.org