

Safety First: Expanding the Global Financial Safety Net in Response to COVID-19

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Abstract

We call for strengthening the Global Financial Safety Net (GFSN) to manage the economic effects of COVID-19, in particular the massive capital outflows from emerging market and developing economies EMDEs and the global shortage of dollar liquidity. Both the United Nations (UN) and the International Monetary Fund (IMF) estimate that EMDEs need an immediate \$2.5 trillion, yet the financing available to them is just \$700 to \$971 billion. To meet these immediate needs we propose to: (1) broaden the coverage of the Federal Reserve currency swaps; (2) issue at least \$500 billion of special drawing rights through the IMF; (3) improve the IMF's precautionary and emergency facilities; (4) establish a multilateral swap facility at the IMF; (5) increase the resources and geographic coverage of regional financial arrangements; (6) coordinate capital flow management measures; (7) initiate debt restructuring and relief initiatives; and (8) request that credit-rating agencies stop making downgrades during the emergency. It argues that leaders should swiftly move to address these structural gaps in the GFSN: (1) agree on a quota reform at the IMF; (2) create an appropriate sovereign debt restructuring regime; (3) expand surveillance activity; and (4) adopt IMF governance reform and strengthen its relations with all agents of the GFSN. All of these reforms must be calibrated toward a just transition to a more stable, inclusive, and sustainable global economy.

COVID-19 highlights the need to strengthen the global financial safety net

The outbreak of COVID-19 is a strong human tragedy that rapidly became an economic tragedy as well. As the world's health systems are under strain to combat the virus, the present 'safety net' to back up the financial system is inadequate to the task. It is still too early to estimate the overall damage, but the immediate economic and financial impacts are unprecedented and on a global scale. A high degree of uncertainty and an initial lack of coordinated policy responses intensified market panic and volatility, resulting in a flight for safety that led to the largest outflow of portfolio capital from emerging market and developing economies (EMDEs) in history and a global shortage of dollar liquidity.

The COVID-crisis has threatened the stability of the global financial system and put to test the institutions and mechanisms that were established to support countries facing liquidity crises. The crisis has shown that the protection that the current multi-layered Global Financial Safety Net (GFSN) – comprising the nations' foreign reserves, central banks' bilateral swap lines, and financial resources of global financial institutions, particularly of the International Monetary Fund (IMF) and the regional financial arrangements (RFAs) – can provide is insufficient to deal with a crisis of current proportions.

While the central banks and governments of most advanced economies have been able to utilize the maximum space for monetary and fiscal policies, most EMDEs have limited room for fiscal and monetary expansion and at

the same time struggle with the highly destabilizing consequences of the sudden reversal of capital flows and some of them from the downgrades from credit-rating agencies. Furthermore, the vast majority of EMDEs have no access to the swap arrangements that the advanced economies provide.

Since the crisis began to unfold, EMDEs experienced a large initial withdrawal of close to \$100 billion, and over 100 countries have gone to the IMF for support. Although private capital markets for EMDEs have opened up since mid-April, access has been very uneven, with only countries that are considered to be 'credit-worthy' by private creditors being able to issue bonds on good conditions. Separate estimates by the IMF and the United Nations Conference on Trade and Development (UNCTAD) see the need for EMDEs to be at least \$2.5 trillion (Georgieva, 2020; UNCTAD, 2020; Wheatley, 2020). The currently available resource base of the IMF and the RFAs only amounts to \$1.5 trillion, with a maximum of \$700 billion to somewhat less than \$1 trillion available to EMDEs, and are thus inadequate to meet the needs of these countries.

In this short article, we discuss the shortcomings of the current system and develop a set of immediate and intermediate proposals to expand and reform the GFSN that will help both the crisis response as well as the development of a more robust and functional global financial system. Our immediate proposals are to expand central bank swap networks, issue at least \$500 billion in special drawing rights, improve the IMF's precautionary and emergency facilities, establish a multilateral swap facility at this institution, expand RFAs, coordinate capital flow management measures, enable debt restructuring and relief, and request that credit-rating agencies stop making downgrades during the emergency. The structural reforms that we propose are to agree on a quota reform at the IMF, create an appropriate sovereign debt restructuring regime, expand surveillance activity, and adopt IMF governance reform and strengthen its relations with all agents of the GFSN.

These emergency measures and broader reforms will help maintain exchange rate stability, and lessen sovereign debt burdens, which in turn will help maintain the financial stability and fiscal space necessary for EMDEs to face the effects of the pandemic and continue to transition toward more socially inclusive and lower carbon economic development.

The limits of the GFSN

The GFSN is a multilayered set of instruments and institutions that create a loose patchwork across the world. A well-functioning GFSN needs to excel at surveillance, preventive and precautionary measures, and liquidity provision and balance of payments support. It is widely held that the GFSN is still highly incomplete, and that the current crisis has exposed many of the limitations in the system.

The first concern is that the GFSN lacks the resources to stem the current crisis. Bilateral currency swaps from the Federal Reserve of the United States are useful to maintain the dollar system and typically amount to short term lending to central banks, but only two EMDEs (Brazil and

Mexico) have access to such swaps.¹ IMF and RFA lending is typically for reserve management for exchange rate management, balance of payments support, and other goals.

Listed in Table 1, the regional and multilateral components of the GFSN hold roughly \$1.5 trillion in capital. The GFSN is thus just 1.8 per cent of global GDP and 0.4 per cent of total global financial assets as measured by the Financial Stability Board (FSB, 2020). Table 1 shows that just under \$700 billion is available for EMDEs. That amount could rise to as much as \$971 billion, but it is unlikely. Members of the IMF can borrow up to a cumulative 435 per cent of their share and even more under an 'exceptional access' lending window such as what was granted to Argentina in 2018. If all EMDEs requested their maximum potential funding from the IMF (and no OECD members except Chile, Colombia, Mexico, South Korea, and Turkey did) that would amount to roughly \$1.1 trillion in potential lending, but the IMF could only fund \$971 billion given its current capital base (IMF, 2020a). With the immediate need for EMDEs totaling \$2.5 trillion, the GFSN falls significantly short in being able to perform its most basic function.

The GFSN has not evolved by design, but rather as a patchwork of institutions and instruments, several of which have arisen in response to the unmet needs of the system that a sequence of crises has made evident. A well-functioning GFSN would need a coordinated set of engagements that can identify financial instability and risk (commonly referred to as 'surveillance'), and provide precautionary and preventive instruments, as well as facilities to mitigate financial instability when it comes.

These functions are performed across four layers of the global system. Table 2 provides an illustrative list of the four layers of the GFSN and the major instruments used across the spectrum. Table 3 exhibits some of the gaps and limitations in the system.

While the GFSN is often described as having 'layers', that does not imply that countries sequentially move from one layer to the next, nor that they have all four layers at their disposal. Indeed, many countries only have the IMF, while a small handful have access to all four. With that important point in mind, the first layer of the GFSN is the realm of national governments and central banks that provide their own surveillance, precautionary measures, and contingency policies. Because the major source of financial instability comes in the form of external shocks related to volatile capital flows, climate change, and now pandemics, national level surveillance is sufficient by itself to identify sources of fragility that will impact their economies. Beginning in the 1990s, after the crises and controversial IMF responses in East Asia and elsewhere, many countries decided to 'self-insure' their economies by accumulating foreign exchange reserves and using capital flow management measures (CFMMs) and macroprudential policies (as they pertain to foreign exchange markets) to prevent and mitigate crises at a national level (Gallagher, 2015; Ghosh et al., 2012; Ocampo, 2017). These policies can have very positive results and give nations the most autonomy in their route to prevent and mitigate crises, but research has shown that their

Table 1. RFA and IMF resources and EMDE's share in lending capacity

	Capital/ swap amount (billion USD)	EMDE's share of lending capacity
International Monetary Fund	971.1	388.5
European Stability Mechanism	90.6	0.0
Chiang Mai Initiative Multilateralization	240.0	201.6
Contingent Reserve Arrangement	100.0	85.0
European Financial Stabilisation Mechanism	67.7	0.0
EU Balance of Payments Facility	54.1	0.0
North American Framework Agreement	14.0	0.0
Eurasian Fund for Stabilization and Development	8.5	8.5
Arab Monetary Fund	3.6	4.7
Latin American Reserve Fund	2.9	4.7
European Macro-Financial Assistance Facility	2.0	0.0
South Asian Association for Regional Cooperation	2.0	2.0
Total	1,556.5	695.0

Note:: Capital/swap amount (billion USD) compiles the paid-in capital of the IMF and the RFAs across the GFSN. The EMD share of lending capacity identifies the EMD share of current lending capacity across RFAs and the IMF as permitted under their charter agreements, though this is constrained by the lending capacity of these institutions.

Source: Compiled by authors drawing from Mühlich et al. (2020), Kring and Gallagher (2019), Henning (2020), IMF (2020), and the annual reports of various institutions.

effectiveness can diminish over time for a variety of reason. What is more, by purchasing trillions of low-yield developed countries' assets, this insurance strategy amounts to an enormous transfer of wealth from EMDEs to more advanced economies at a high opportunity cost to productive domestic investment (Ocampo, 2017).

Certain nations also have access to bilateral credit lines and swaps, which form the second layer of the GFSN (Mehrling, 2015). The United States Treasury is home to the Exchange Stabilization Fund that disbursed numerous loans and swaps to Mexico in the 1990s, and Japan and Russia provided bilateral credit to neighboring countries during the same period (Grimes, 2009; Henning, 1999; Katada, 2001; Schneider and Tobin, 2020). The crisis of 2008–09 and the succeeding Eurozone crisis led to a significant use of swap lines with no *ex post* conditionality. In addition, the People's Bank of China has signed numerous swap agreements with other countries since 2008.

Table 2. Instrumentation across the global financial safety net

	Precautionary Platforms	Liquidity Provision
National governments	Micro- and macro-prudential regulation Foreign currency reserves Capital flow management measures	Fiscal and monetary policy Foreign currency reserves
Bi-lateral arrangements	Bi-lateral swap arrangements Bi-lateral credit facilities	Activation of bi-lateral swaps Drawing on credit facilities
RFAs	CMIM swap arrangements CRA swap arrangements NAFA swap arrangements SAARC swap arrangements	CMIM activation of swaps CRA activation of swaps NAFA activation of swaps SAARC activation of swaps ArMF credit facilities ESM credit facilities FLAR credit facilities EFSD credit facilities
Multilateral facilities	IMF Flexible Credit Line IMF Precautionary and Liquidity Line	IMF Stand-by Arrangements IMF Extended Fund Facility

Acronyms: ASEAN + 3 Macroeconomic Research Office (AMRO), Chang Mai Initiative Multilateralisation (CMIM), Arab Monetary Fund (ArMF), European Stability Mechanism (ESM), Contingent Reserve Arrangement (CRA), North American Framework Agreement (NAFA), Latin American Reserve Fund (FLAR), South Asian Association for Regional Cooperation (SAARC), Eurasian Fund for Stabilization and Development (EFSD), Bank for International Settlements (BIS), Financial Stability Board (FSB).

Source: Compiled by authors drawing from Kring and Gallagher (2019), Henning (2020).

Rather than hegemonic provision of public goods, many countries are concerned that the allocation of bilateral swaps is uncertain, incomplete, and asymmetric. They are concerned that they do not have access to this type of support – either because they do not qualify given *ex ante* conditionality criteria or more arbitrary geopolitical criteria (Aizenman and Pasricha, 2010; Ocampo, 2017; Volz, 2016). The joint announcement in March 2020 by the Bank of Canada, the Bank of England, the Bank of Japan, the European Central Bank, the Federal Reserve, and the Swiss National Bank to enhance the provision of liquidity among each other via the standing US dollar liquidity swap line arrangements is an important contribution to the

Table 3. Gaps and limitations in the global financial safety net

	Surveillance	Precautionary platforms	Liquidity provision
National governments	Limited attention to national-global links Lack of reliable information	Inadequate currency reserves Weak efficacy of prudential measures Limited efficacy of CFMMs	Limited efficacy and availability of fiscal/monetary policy Lack of level and efficacy of currency reserves
Bi-lateral arrangements	Largely absent of formal surveillance activity	Asymmetric and uncertain availability Ex-ante conditionality concerns	Asymmetric and uncertain availability Ex-ante conditionality concerns
RFAs	Incomplete geographic coverage Narrow thematic coverage	Limited level and coverage of swaps Linkages to the IMF	Limited level and coverage of swaps Linkage to the IMF
Multilateral facilities	Uneven quality of IMF surveillance Narrow thematic coverage (IMF surveillance) Limited attention to global-country specific links (FSB/BIS)	Absence of multilateral swap facility Inadequate level of IMF resources available Stigma attached to IMF credit lines Ex-ante conditionality of IMF facilities	Inadequate level of IMF resources available Lack of IMF voice and representation by EMDs Pro-cyclical conditionality of IMF programs Stigma & mixed outcomes of IMF programs

Source: Compiled by authors.

management of the crisis, but also illustrates the fact that the vast majority of economies are excluded from similar lines of defense. The Federal Reserve subsequently established temporary dollar liquidity-swap lines with nine additional central banks, including two EMDEs. The more recent move by the Federal Reserve to establish a foreign and international monetary authorities' facility (FIMA Repo Facility) is also a step in the right direction, but will largely benefit just a handful of EMDEs also holding significant reserves.

A third layer of support is provided by RFAs that take the form of either swap arrangements (such as the Chang Mai Initiative Multilateralisation (CMIM), and the BRICS Contingent Reserve Arrangement) or credit facilities (such as the Latin American Reserve Fund, the European Stability Mechanism, and the Arab Monetary Fund). While RFAs are more flexible and have more 'ownership' over their policies, they lack adequate levels of capital and those that require a parallel IMF program are not sufficiently used because of the general stigma associated with IMF conditionality (McKay et al., 2011). Thus, with the exception of the Eurozone's extensive use of the European Stability Mechanism (ESM) and some countries' use of the Latin American Reserve Fund, FLAR (which has no formal conditionality), the other RFAs remained dormant during the recent crises in favor of swaps or self-insurance (Kring and Grimes, 2019). Although many of the RFAs, especially CMIM (through the ASEAN + 3 Macroeconomic Research Office (AMRO)) and FLAR, have developed sophisticated surveillance activities that are more attuned to understanding how capital flows will impact regional stability, their limited mandates, size, and capacity

have prevented them from expanding their purview to examine new shocks associated with climate change and health pandemics (Grabel, 2017). What is more, a large number of countries across the world simply lack any access to an RFA at all (Mühlich and Fritz, 2018; Volz, 2016).

Most nations in need only have the fourth and only multilateral layer, the IMF. IMF surveillance efforts have been assessed by its own Independent Evaluation Office to be lacking in that they failed to anticipate the instabilities preceding the 2008–09 financial crisis (IMF-IEO, 2014, 2019). The IMF was strengthened after the 2008–09 crisis, including through the creation of a range of multilateral surveillance instruments. Only recently has the IMF focused on global climate change, with landmark issues of the *Fiscal Monitor* and the *Global Financial Stability Report* on this issue (IMF, 2019a, 2019b). The IMF has also started to consider pandemic and health security as a risk factor in Article IV consultations, but such risks have not yet been formally integrated into its country analysis (World Bank Group, 2019). The IMF is only now starting to officially incorporate these important sources of financial shocks into its analyses of the financial systems of member countries.

The IMF created a host of precautionary facilities that were potentially more flexible, including the Flexible Credit Line and the Precautionary and Liquidity Line (IMF, 2017b). These new facilities received little use because of the strict *ex ante* conditions involved in qualifying for the first of them (Marino and Volz, 2012). Thus, nations often had no choice but to resort to traditional facilities, particularly the stand-by arrangements, which remained highly conditional,

frequently include contractionary macroeconomic policies, and have a mixed record when it comes to crisis recovery and social outcomes (Kentikelenis et al., 2016).

There are also significant concerns about voice and representation of all members of the IMF and delays to regular quota reviews (Gao and Gallagher, 2019; Ocampo, 2017). It took six years for the 2010 quota increases and redistributions of votes at the IMF to be adopted. Further, it is worrisome that efforts to follow-up with new reforms on quotas and votes were delayed until 2023. Although the IMF is tasked to follow a 'doctrine of economic neutrality' (Swedberg, 1986), case studies and statistical analysis have found that lending decisions (including loan conditionality) often reflected the geopolitical and economic interests of G7 countries in general and the US in particular. Looking at the IMF, Thacker (1999), Stone (2002, 2011) and Copelovitch (2010a, 2010b) find this pattern, whether looking at countries known to be important to the US at the time, or analyzing key United Nations General Assembly votes. Dreher et al. (2009, 2010, 2015) find this favoritism extends to IMF lending, and Dreher et al. (2018) are able to link it specifically to UN Security Council voting records.

Proposals for expansion and reform of the GFSN

The G20 and IMF have previously called on members and beyond to strengthen the GFSN and 'promote a resilient international monetary and financial system, including by reconsidering elements of the IMF's lending toolkit and deepening collaboration with regional financing arrangements.' (G2019, 2019; IMFC, 2019). To this end, we propose eight immediate measures and a four-point agenda to address the structural gaps of the current GFSN:

1. Broaden the coverage of Federal Reserve swaps. In response to the outbreak of the pandemic, the Federal Reserve took immediate action, first lowering the funding cost of its swap lines signed with five other central banks, and then extending the dollar swap lines to nine more central banks in order to meet the surging demand for dollar liquidity. Such emergency assistance would certainly help lessen strains in global dollar funding market for some specific jurisdictions. In the immediate term, the swap lines of the Federal Reserve should be extended to at least the People's Bank of China, the world's largest trading partner but also spread to others EMDEs.
2. Issue at least \$500 billion of IMF Special Drawing Rights (SDRs). The IMF board should approve an allocation of SDRs of at least \$500 billion. Close to two-fifths of such an allocation would enhance the international liquidity of EMDEs, which are the primary users of SDRs. A decision should also be adopted by which high-income countries would lend to the IMF the SDRs that they do not use, to enhance the Fund's lending capacity.
3. Improve the IMF's precautionary and emergency facilities. It is also important to improve the access and flexibility of existing tools, such as the IMF Flexible Credit Line and Precautionary and Liquidity Line for tackling potential balance of payments pressures. Even more importantly, access and funding for the emergency facilities – the Rapid Financing Instrument (RFI) and Rapid Credit Facility (RCF) – must be improved to face the urgent needs arising from the pandemics, but also from commodity price shocks, conflict situations and natural disasters.
4. Establish a multilateral swap facility at the IMF. Equally important is for the IMF to establish a multilateral swap facility that would be open and unconditional to all countries. This has been elaborated on by the IMF staff, with earlier versions have been proposed by experts and the G-20 Eminent Persons Group (de Gregorio et al., 2018; IMF, 2017a; Truman, 2010). This could be funded by an SDR allocation, again with countries not using their allocations making the funds available to the IMF to finance such a facility. In 2017, a proposal for such a facility was rejected in the IMF Board by a minority of creditor shareholders that have a disproportionate share of voting rights at the IMF, but it is 'shovel ready' in design.
5. Increase the resources and geographic coverage of RFAs. The existing resources of the RFAs in EMDEs need a step-wise increase, and a geographic expansion. Many countries lack access to a variety of swap and credit lines at the regional and multilateral level. The most glaring gap in RFAs is Africa. Though a number of African countries have signed on to a new African Monetary Fund, many countries are yet to sign on and then they need to ratify the articles of agreement. This proposal and specific design is also 'shovel ready' and in need of ratification and funding (Dagah et al., 2019). This should be done immediately. Significant gaps also exist in South and Central America and the Caribbean, Eurasia, and South Asia. Also, and notably, some G20 countries, like Argentina and Turkey, are not covered by RFAs at all.
6. Coordinate capital flow management measures (CFMMs). As the world puts these other measures in place, EMDEs should regulate the outflow of capital in order to protect their balance sheets and exchange rates – and to moderate inflows during 'surges' of capital. These ideas date back to the origins of the IMF and are implied in the articles of agreement and are now becoming mainstreamed in economics and international institutions (Gallagher, 2015; Helleiner, 1990). With the IMF's 'institutional view' on CFMMs adopted in Helleiner (2012), such an approach is now accepted as part of the toolkit for situations like the one we are in, and should be acted upon when necessary (Gopinath, 2019; IMF, 2012).
7. Debt restructuring and relief. Even with a rapid and significant expansion of liquidity and balance of payments support to EMDEs, a substantial amount of debt will need to be written off. The IMF has already noted that Argentina – the recipient of the largest IMF program – will need a significant debt restructuring (IMF, 2020b), and the World Bank and IMF have called for bi-lateral debt relief for the poorest countries. UNCTAD (2020), suggests that \$1 trillion in developing country debt will need to be alleviated in 2020 across multi-lateral and bi-lateral debt classes. The United Nations has agreed upon a

resolution setting forth a set of principles for sovereign debt restructuring processes that can be built upon (United Nations, 2015).

8. Credit-rating agencies must stop making downgrades during the emergency. Downgrades by credit-rating agencies are generating additional pressures on capital flight from emerging economies. They should pause as markets settle and prices adjust so as not to accentuate the present volatility and uncertainties. In the meanwhile, credit-rating agencies should also work on their business models to improve their surveillance of financial market volatility and further integrate vulnerabilities associated with pandemics and climate change.

After these immediate measures, in the intermediate term over the course of the next eighteen months, leaders will also have to address the following structural gaps in the GFSN:

1. Quota Reform at the IMF and expansion of RFA resources. The resources available through the GFSN need to be expanded. Members of the IMF and RFAs should provide significant new resources for new facilities. Quota-based increases should form the core of IMF resource mobilization, and the 16th Quota Review should be adopted in 2020, and mandate stepwise quota increases and a redistribution of quota and voting shares. Existing and newly created RFAs should be scaled up in a stepwise manner as well.
2. Create an appropriate Sovereign Debt Restructuring Regime. The international financial architecture still lacks an adequate workout system for the restructuring and reprofiling of sovereign debts, as has come painfully clear in the recent case of Argentina (IMF, 2020b). Existing mechanisms to renegotiate sovereign debts with private creditors have improved but are inadequate because of the multiplicity of debt contracts, some of which are still not subject to collective action clauses. A global institutional mechanism to renegotiate sovereign debts should be put in place as soon as possible. EMDEs were already close to unsustainable debt levels due to the surge in private capital flows in recent years, and many of those debts will be unsustainable with the massive capital flight and exchange rate depreciation that have taken place.
3. Expand surveillance activity. All GFSN institutions should expand their surveillance activities to focus on the new drivers of shocks, particularly spillovers generated by the monetary policies of advanced countries, volatile short-term capital flows, cross-border digital asset movements, global climate change, and health pandemics. In particular, it is necessary to highlight the importance of surveillance of macroeconomic and financial conditions that generate the risk of crises.
4. Governance reform. The IMF and other parts of the GFSN should reform their governance structures and cooperate in a manner that provides global public goods without jeopardizing national policy sovereignty. The IMF, with its broad membership, remains the global multilateral body that provides predictability to liquidity needs in the global economy. Echoing G20 principles, the IMF should work

with central banks and RFAs in a manner that respects the roles, independence and decision-making processes of each institution, taking into account regional specificities in a flexible manner (G2019, 2019; McKay et al., 2011; Report of the G20 Eminent Persons Group on Global Financial Governance, 2018; Volz, 2013). These institutions should cooperate closely during crises while allowing for complementarity and diversity of approaches to governance, surveillance, program design, and conditionality over the longer run. They should create mechanisms for greater international policy coordination managing capital flows across regions and between EMDEs and advanced economies (Ostry et al., 2012). Moreover, the IMF should work to ensure that trade and investment regimes also allow ample policy space for national efforts and international cooperation on capital flow management. Such treaties increasingly restrict the capacity of countries to manage capital flows. The IMF has recognized that 'these agreements in many cases do not provide appropriate safeguards or proper sequencing of liberalization, and could thus benefit from reform to include these protections' (IMF, 2012, p. 8; Gallagher et al., 2019).

Obstacles to reform efforts

While the G20 and the IMF have long called for reforms to the GFSN, reform and even substantive engagement between the different layers of the GFSN has been slow to materialize. The current COVID-19 crisis presents both an urgent need for immediate reforms to the GFSN to mitigate the ravaging economic effects of the pandemic and an opportunity to strengthen, expand, and better integrate the various components of crisis finance. But just because a crisis has created an opening, it does not mean that substantive change will materialize.

At the moment, the current US Administration has underestimated the nature and effects of the pandemic and has taken several steps to weaken or abandon multilateralism. Likewise, Europe has grappled with internal strife in the form of Brexit and underwent conflictive negotiations until reaching an agreement on regional cooperation in July. In short, both domestic and regional political cleavages and diverging views on how to respond to COVID-19 at the national level provide significant obstacles to multilateral efforts. That said, the demands generated by the crisis create both an opening for reform of the GFSN and the salient need to bolster and better coordinate crisis financing entities.

Some areas of much-needed reform may have greater chance of success than others. The effects of the COVID-19 crisis on public finances and public debt sustainability will inevitably force a long-overdue discussion on the restructuring and reprofiling of sovereign debts, providing an opportunity for making progress in this policy area. Also, the rapid and hands-on reaction of the IMF during the current crisis, and the fact that its emergency support came without conditionality, helped dispel concerns of crisis-affected countries about engaging with the Fund. It may also open the door to closer collaboration between the IMF and RFAs. The magnitude of

the economic effects of the pandemic has also led the IMF to realize that it needs to expand surveillance activity by monitoring risks beyond the traditional macro-financial risks it has focused on thus far. In particular, the crisis has highlighted how weak health and social systems undermine economic resilience, which are therefore also becoming increasingly recognized as being macro-critical for the Fund's work. Other areas or reform, including quota and governance reform, will see little progress unless the major shareholder countries, and the US administration in particular, adopt a more cooperative stance to multilateral governance.

Concluding remarks

The COVID-19 crisis has highlighted the underlying weaknesses of the GFSN. The GFSN needs to be enhanced through measures that will enable the world to contain crisis like COVID-19, to save lives and jobs, calm markets, and steer finance toward a more adept, sustainable, and inclusive world economy. The world shares a common but differentiated responsibility to prevent destructive unilateral economic actions that prevent other nations from realizing these common goals, while maintaining the right to pursue national development strategies and advancing global public goods (Gallagher and Wright, 2020).

The IMF, RFAs, and national entities need to align these efforts with the SDGs, the Addis Ababa Action Agenda on Financing for Development, and the Paris Agreement on Climate Change. Despite recognized improvements in the number of conditionalities explicitly required in IMF programs, in particular the possibility of countries under the programs to preserve spending 'floors' for social programs, IMF conditionalities still carry a stigma because of their procyclical nature and social impacts. While the academic literature on the impacts of IMF programs on economic growth is somewhat mixed, there is overwhelming evidence in the literature that IMF conditionality is correlated with worsening educational spending, health systems, inequality and environmental quality (IMF, 2018; Kentikelenis et al., 2016). The flexible response of the IMF to the COVID-19 crisis and the recognition of the crucial importance of functioning health and social systems for an effective response to pandemics may indicate a shift in IMF policies in this respect, and may lead to a weakening of the stigma associated with borrowing from the IMF. More broadly, the crisis may herald new thinking among the various stakeholders of the GFSN to better prepare for the challenges of the future, which will inevitably differ from those of the past.

Our proposals for financing for the immediate liquidity needs of the world economy can enable EMDEs to reduce exchange rate instability, limit indebtedness, and maintain the fiscal and financial space to attack the virus while transitioning the world economy to a more sustainable and inclusive one. COVID-19 does not discriminate between rich and poor countries, but the GFSN does, in that its coverage is uneven and disproportionately supports developed countries. These inequities mean that the COVID-19 induced financial crisis is likely to disproportionately impact EMDEs.

At the same time, the crisis presents an opening for bold thinking, innovation, and action. All solutions have trade-offs and limitations, but these proposals constitute an ambitious 'whatever it takes' strategy that is aligned with the SDGs, the Addis Ababa Action Agenda and the Paris Agreement.

Note

1. The Republic of Korea and Singapore, which some analysts include in the emerging market economy bracket even though they are already high-income countries, were also granted swap arrangements with the Fed.

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