NATIONAL INTEREST ANALYSIS: CATEGORY 1 TREATY

Loan Agreement between Australia and the International Monetary Fund

[2020] ATNIA 10
[2020] ATNIF 13

Nature and timing of proposed treaty action

1. The proposed treaty action is the entry into force of the *Loan Agreement between Australia and the International Monetary Fund* (the Agreement). The Agreement will renew and adjust a line of credit that Australia currently extends to the International Monetary Fund (the IMF).

2. The Agreement will enter into force on the date that the IMF acknowledges receipt of a written communication from Australia stating that Australia has met all of its domestic requirements in regards to the entry into force of the Agreement or on January 1, 2021, whichever is later (paragraph 15(b)). Australia will send the notification as soon as practicable following the completion of domestic treaty-making requirements. The term of the Agreement will end on 31 December 2023, and is extendable by one year through to 31 December 2024 with Australia's consent (paragraph 2(a)).

3. The proposed treaty action will replace an existing loan agreement between Australia and the IMF (the existing Agreement). The existing Agreement entered into force for Australia on 13 July 2017 and will expire on 31 December 2020.

4. The Agreement has not yet been signed by both parties, however the IMF Executive Board have provided Australia with consent for tabling prior to signing through endorsement of their decision on the paper on 2020 Borrowing Agreements—Status of Discussions and First Set of Agreements—Supplementary Information and Revised Proposed Decision (EBS/20/132, Supplement 1) on 31 July 2020.

Overview and national interest summary

5. The Agreement is a bilateral borrowing agreement (BBA) that enhances the resources available on a temporary basis to the IMF for crisis prevention and resolution through bilateral borrowing (paragraph 1(a)).

6. The IMF derives its resources for lending to member countries from its permanent resource base (provided through quota contributions from member countries) and temporary borrowing arrangements (held with a subset of member countries and institutions). These temporary resources include BBAs and the New Arrangements to Borrow (NAB) (a multilateral credit arrangement), and currently comprise around half of the IMF's total lending capacity.

7. The IMF is seeking to renew BBAs with up to 40 member countries (including Australia) and to double the aggregate size of the NAB, ensuring the overall size of the IMF's temporary resources remains unchanged.

8. The Agreement will have an initial credit amount that will oblige Australia to lend the IMF the equivalent of up to Special Drawing Right (SDR) 4.61 billion (approximately A$9.04 billion as at 29 July 2020) under specific circumstances. However, a reduced credit amount SDR 1.986 billion (approximately A$3.90 billion as at 29 July 2020) would come into effect once Australia's NAB credit arrangement is doubled under the NAB reform. The NAB is a separate agreement, however the credit arrangements between both the NAB and the Agreement are being considered as part of Australia's overall contribution to the IMF. Amounts lent under the Agreement will be repayable in full and with interest paid at the IMF's SDR interest rate.

9. It is in Australia's interest that the IMF remains strong, adequately resourced, and at the centre of the global financial safety net. The IMF plays a vital role at the centre of the global financial safety net and is responding to the COVID-19 crisis with unprecedented speed and magnitude of financial assistance. In particular, the IMF is providing emergency financing and debt relief, as well as enhancing liquidity and adjusting existing programs and access limits to ensure countries have the capacity to effectively respond to the health and economic crisis caused by COVID-19.

Reasons for Australia to take the proposed treaty action

10. Australia benefits from an effective IMF that has the resources available to fulfil its mandate to support global economic and financial stability. The IMF is the central institution of a global financial safety net that promotes international financial and monetary stability by encouraging global monetary cooperation and providing a credible financial backstop for countries in economic difficulty.

11. Given the current climate with the impact of COVID-19 and risks to the global economic outlook, confidence in the IMF's ability to respond to this crisis is critical in maintaining the confidence of economic participants to continue to invest and trade. The experience of the Global Financial Crisis indicates that it is important that the IMF has sufficient financial resources in place to respond to the COVID-19 pandemic with speed and magnitude to assist countries facing liquidity and balance of payments issues resulting from this crisis.

12. It is in Australia's interest to ensure the IMF's total lending capacity as part of the global financial safety net is not diminished and the Agreement is part of securing this capacity.

13. Funding through multilateral means such as the Agreement also ensures that Australia can contribute in an efficient and effective manner by providing a relatively small portion of financing to a much larger pool that can be drawn on by member countries. This reduces the likelihood that Australia will need to provide direct finance to countries bilaterally that would likely require much larger sums of funding and more credit risk.

14. Any default risk to Australia will be minimal as the IMF borrows from its creditor members with the backing of its full balance sheet and ultimately the resources of its global membership.

Obligations

15. The Agreement requires Australia to lend the IMF up to SDR 4.61 billion (approximately A$9.04 billion as at 29 July 2020) (paragraph 1) under specified conditions. This amount will be reduced to the equivalent of up to SDR 1.986 (approximately A$3.90 billion as at 29 July 2020) upon the increase in Australia's credit arrangement under the NAB.

16. This obligation to lend will come into effect if and when the Agreement is activated. Activation will occur through a two-step process. First, the IMF's capacity to lend to member countries from quotas and the New Arrangements to Borrow must fall below SDR 100 billion. Then, the IMF must obtain agreement from creditor countries representing 85 per cent of the value of all bilateral loan agreements that the IMF has entered into or amended pursuant to the borrowing framework approved by the IMF in March 2020 (who are eligible to vote in accordance with certain terms and conditions (paragraph 2(b)).

17. The IMF may seek a drawdown of funds from creditor countries (including Australia) even though its available resourcing is above the SDR 100 billion threshold if extraordinary circumstances warrant it in order to forestall or cope with an impairment of the international monetary system (paragraph 2(b)).

18. In accordance with specific criteria and conditions, the IMF's ability to seek drawings under the Agreement will also be determined by Australia's current and prospective balance of payments and reserve position (paragraph 3(a)).

19. The IMF will provide advance notice of its best estimate for the amount it expects to draw under the Agreement (paragraph 3(a)). The IMF will repay amounts drawn within three months of the drawing date, extendable at the IMF's discretion in three month increments to a maximum of ten years (paragraph 5(a)). In exceptional circumstances as a result of a shortage of IMF resources, the IMF, with Australia's agreement, may extend the maximum maturity of drawings by up to a further five years (paragraph 5(a)). The rate of interest on drawings will be the SDR interest-rate (paragraph 6(a)). In accordance with Rule T-1 of the IMF By-Laws, the SDR interest-rate is determined weekly, based on a weighted average of representative short-term money market interest rates (currently the US dollar, Euro, Pound Sterling, Yen and Renminbi rates).

20. Australia may also obtain early repayment of all or a proportion of outstanding drawings if there is a need arising from its balance of payments and reserve position (paragraph 8). Australia will also be able to transfer all or part of any claim on the IMF resulting from outstanding drawings to any IMF member country, subject to limitations set out in the Agreement (paragraph 9(b)).

21. The IMF will still have the right to drawdown funds from Australia under the existing Agreement for commitments made by the IMF during the term of that agreement. In this circumstance, aggregate outstanding drawings by the IMF under both agreements will be limited to their common maximum borrowing limit of SDR 4.61 billion (approximately A$9.04 billion as at 29 July 2020), or new maximum borrowing limit of SDR 1.986 billion (approximately A$3.90 billion as at 29 July 2020) in case of the effectiveness of the new NAB (paragraph 14(e)).

Implementation

22. The *International Monetary Agreements Act 1947* (IMA Act) provides a standing appropriation and legislative framework that gives the relevant authority to borrow and lend in place to allow the Australian Government to meet its obligations under the Agreement with the IMF (from 1 January 2021).

23. Paragraphs 8CAB(1)(a) and(b) of the IMA Act states that the Minister may, on behalf of Australia, enter into one or more agreements with the Fund that: provide for Australia to provide loans to the Fund; and contain terms and conditions determined by the Minister.

Costs

24. The Agreement will be included in the budget papers as a quantifiable contingent liability. The IMF can draw on the Agreement only when additional funds are required to support its lending to member countries, up to a maximum of SDR 4.61 billion (approximately A$9.04 billion as at 29 July 2020), or SDR 1.986 billion (approximately A$3.90 billion as at 29 July 2020) in the case of the effectiveness of the new NAB. The Agreement is not expected to be drawn upon over the forward estimates as the IMF's current available resources are sufficient to cover its projected lending activities.

25. Any drawings would be financing transactions. The loan agreement would have an indirect impact on the underlying cash balance if the agreement is activated and funds are provided. This impact would arise where the Australian Government's lending to the IMF increased Australia's own borrowing requirement and where the interest payable on any money borrowed by Australia to meet an IMF drawdown differs from the interest paid by the IMF in regard to that drawdown.

Future treaty action

26. The Agreement does not make express provision for amendments. Any future amendments to the Agreement will be subject to Australia's international obligations and its domestic treaty-making requirements.

27. The IMF may extend the Agreement by one further year, through to December 31, 2024 by a decision of the Executive Board, taking into account the Fund's overall liquidity situation and actual and prospective borrowing requirements, and with the consent of Australia (paragraph 2 (a)).

Termination

28. The Agreement will expire on December 31, 2023, with the possibility of a one-year extension to 31 December 2024, with Australia's consent (paragraph 2(a)).

29. The Agreement does not contain a specific right of termination for either party.

Contact details

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Treasury

ATTACHMENT ON CONSULTATION

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CONSULTATION

30. The Agreement is judged to have a negligible impact on the States and Territories and no State or Territory Government representatives were directly engaged in considering the Agreement.

31. The Agreement is judged to have a negligible impact on external stakeholders and none were directly engaged in considering the Agreement.