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Multilateral development banks in Latin America

Recent trends, the response to the pandemic, and the forthcoming role

Pablo Fleiss

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Contents

Tables

Figures

Boxes

Maps

Abstract

The COVID-19 crisis has hit Latin America and the Caribbean harder than any other developing region. In 2020 the regional GDP will experience its greatest decline in 120 years. The pandemic represents a formidable social challenge, exposing all the regions' endemic problems. Against this backdrop, this paper analyses the Multilateral Development Banks (MDBs) response to the COVID-19 crisis and their post-pandemic role and prospects in LAC. Some basic information is presented on the major MDBs that serve the region and their main trends during the last decade to provide an adequate context. Preliminary data indicate that MDBs combined approved approximately $50 billion to the region in 2020. This represents a 25% increase with respect to 2019. In comparison, in 2008, the first year of the Global Financial Crisis, the increase was 45%. While all MDBs expanded their credits to the region in 2020, the size of their respective incremental responses appears to be linked to their differences in equity levels and portfolio-associated risks. The paper closes by sketching some critical factors that will continue to play an important role in the discussions among MDBs in the near future. We identify three major issues: providing anti-cyclical support, maintaining an adequate level of capital, and encouraging strong coordination among MDBs.

Introduction

The COVID-19 crisis has hit Latin America and the Caribbean (LAC) harder than any other developing region. In 2020 the LAC's Gross Domestic Product (GDP) will plunge -7.7% (ECLAC, 2020). That figure represents the greatest decline in 120 years. The regional fall in economic activity significantly exceeds the average drop in developing economies and the world's output, -3.3% and -4.4%, respectively (IMF, 2020). By December 2020, the region accounted for 8.5% of the world's population but almost 20% of cases and 30% of deaths for COVID-19.

This crisis struck a region already in a slowdown. The period 2014-2019 was the one with the lowest growth (0.3% annual average) since the 1950s (ECLAC, 2020). The collapse will make the 2020's GDP per capita similar to the 2010's, turning this decade into another lost decade for the region. Furthermore, recovery will be neither as strong nor as immediate as in other regions. In 2021, the regions' GDP is projected to grow at 3.7%, below developing economies and global averages (6.0% and 5.2%, respectively). The recovery is not expected to bring a return to pre-crisis GDP levels until 2023, and forecasts until 2025 are below the world's average as well (IMF, 2020).

The pandemic represents a formidable social challenge. The crisis exposed all of the regions' endemic problems. The decline in GDP and the expected increase in unemployment rates will raise the number of people living in poverty and extreme poverty by 45 and 28.5 million, respectively (ECLAC, 2020). As a result, more than 230 million people in LAC live in poverty right now. The crisis disproportionally hit low-income households and smaller firms. Informality and inequality will probably rise, countering the progress made in the last decade.

The health and economic crisis will probably lead to debt distress and financial crises. Since the pandemic outbreak, governments worldwide have provided liquidity to businesses and supported households struck by a sudden loss of income and employment. As a result, the public sector will face increased financing needs. On top of the additional health bill and the costs associated with the expected immunization programs, and amid all programs to mitigate the drop in household income, governments will have to confront lower revenues due to economic contraction in the context of already high public debt vulnerabilities. Depending on alternative GDP trajectories and public spending, the average debt in LAC countries could increase by 15 points, reaching 73% of GDP in 2022 on average (Pineda, et al., 2020).

Against this backdrop, this paper analyses the Multilateral Development Banks (MDBs) response to the COVID-19 crisis and the post-pandemic prospects of these institutions in LAC. Some basic information on the major MDBs that serve the region and their main trends during the last decade is presented to provide an adequate context. The Global Financial Crisis (GFC) of 2008-2009 is a useful benchmark to compare multilateral responses during the current crisis. The paper closes with a discussion of issues that will be important in determining how MDBs will adapt to the new global scenario.

MDBs have historically played a significant role in addressing LAC's main regional development challenges, whether social, infrastructure, integration, or climate change. Beyond this structural support, when a crisis hits the region, client countries appeal to MDBs for resources and advice to mitigate the negative shocks' immediate effects, shorten the downfall and strengthen the recovery phase. MDBs have responded accordingly, supporting the region throughout all the previous crises, including the debt crisis of the 1980s, the Tequila and Asian crisis of the 1990s, and the GFC.

Since the aftermath of the GFC and throughout the past decade, some interesting trends have been observed. First, multilateral debt has declined as a percentage of total public debt in the last ten years. This decline resulted from the faster increase in public debt financed by both private creditors through bonds and commercial banks. However, for the smaller and poorer countries, MDBs remain the main source of public finance. Larger economies bear higher exposures to private debt, while some economies have witnessed a surge in bilateral Chinese debt.

Within MDBs, non-sovereign guaranteed flows have increased faster than sovereign guaranteed ones as private-sector lending and mobilization have been placed at the center of MDBs strategies. While LAC has become a middle-income region, concessional lending has fallen. After the GFC, the World Bank reduced its lending to the region, while regional MDBs continued expanding. As a result, lending by regional banks (especially the Inter-American Development Bank, IDB, and the Development Bank of Latin America, CAF) has significantly outpaced that of the World Bank to LAC. MDBs' financial flows have been countercyclical as a whole, and disbursements raise during crises, although cyclicality varies across MDBs. Finally, MDBs face a competitiveness problem regarding their highest-rated borrowers due to their easy access to international financial markets.

In this crisis, while all MDBs have expanded their credits to the region, the size of their respective incremental responses appears to be linked to their differences in equity levels and portfolio-associated risks. Overall, preliminary data indicate that MDBs approved approximately $50 billion in new resources in 2020. This represents a 25% increase with respect to 2019. In comparison, in 2008, the first year of the GFC, the increase in approvals was 45%. On top of that, the International Monetary Fund (IMF) has offered a significant response to the crises in terms of speed and volume. Between 2018 and 2020, the IMF has approved $185 billion in emergency financing, some two times more than the total MDBs' sovereign guaranteed approvals during the same period. IMF's lending has been mainly precautionary and concentrated on six countries.

A robust response requires substantial resources to be made available to their clients. We look into the evolution of equity in each institution to understand why some have acted more vigorously. In 2018-2019 the World Bank Group obtained a capitalization (including a substantial replenishment of the International Development Agency). Moreover, the IDB Invest (the private sector arm of the IDB) and the Central American Bank of Economic Integration (CABEI) also agreed on a capitalization in the last five years. These capital increases allowed each of these institutions to substantially expand their finance to the region in 2020. On the contrary, the last capital increase of the IDB occurred further back in time. The new IDB's president (elected in October 2020) has launched a discussion to increase the capital and expand the annual lending capacity to $20 billion a year. At the CAF, the last capital increase was negotiated in 2015 (the final of four consecutive capitalizations between 2007 and 2015), and it is still receiving contributions.

The paper also discusses the role of Credit Rating Agencies (CRAs) on the MDBs operative. Maintaining high ratings to obtain optimal financial terms to transfer to their clients is key to the MDBs' financial models. Consequently, trying to preserve the highest possible rating is a clear policy mandate of these institutions. Rating considerations constraint MDBs lending, especially during crises, because the CRAs methodologies, which adapt methods designed to assess commercial banks, fail to capture the anticyclical role embedded in MDBs. CRAs methodologies evaluate the portfolio quality and measure it against the bank's equity. In a crisis, the portfolio quality decreases, so more equity is needed to support the same lending level. Hence, a significant rise in lending without a parallel rise in capital may jeopardize MDBs ratings. In this way, CRAs might limit MDBs financing expansion during crises and hinder MDBs anticyclical lending. Risk considerations and CRAs views also matter for debt standstill discussions.

Once analysed the main trends of the last decade and the immediate response to the COVID-19 crisis, the paper closes by sketching some critical topics that will probably play an important role in the discussions among MDBs in the near future. We identify three major issues: providing anti-cyclical support, maintaining an adequate capital level, and encouraging strong coordination among MDBs.

The COVID-19 pandemic reinforced the idea that MDBs play a role in mitigating negative shocks. However, MDBs are not always geared to respond to cycles. An institution's capability to behave countercyclically and expand activities during a descending phase of a cycle is linked to its ability to moderate its approvals and lending during the ascending phase. Managing cyclical lending requires an institutional governance that develops the ability to modify lending rapidly. Moreover, the financial rating criteria to which MDBs are subject does not contemplate their anticyclical role, penalizing their stance during crises and failing to judge the financial health of an MDB throughout the entire cycle. Beyond expanding or contracting the level of resources allocated each year, an important element of MDB's anti-cyclical support is the possibility of offering ex-ante financial support to face crises. While the MDBs have traditionally focused on ex-post emergency lending, they have progressively extended the set of contingent and precautionary loans. These ex-ante instruments involve significant benefits to borrowing member countries.

The pandemic has also highlighted the importance of having MDBs well prepared to confront the current and upcoming crises. The response to the exceptional demands generated by this crisis is stretching the balance sheets of the MDBs. As the size of MDBs' response is linked to the available spaces in their balance sheets and their ability to implement quick changes in their programming, it is important to evaluate how well-equipped the MDBs are. MDBs would need periodical assessments of their capital needs and an agreement on how and under which conditions they require a capital increase. This type of conversation may contribute to the coordination among shareholders, and between them and MDB's management. So far, the launch of the capitalization discussions has been ad-hoc, depending on external dynamics and occasional shareholder appetite. These processes systematization could bring enormous benefits to the multilateral system.

The COVID-19 crisis erupted in a context marked by the resurgence of nationalism and mistrust of the multilateral system. In this context, international cooperation has been limited, and so was the assistance received by developing countries (especially the middle-income ones), contrasting with developed countries' ambitious domestic policies. Coordination among MDBs has become more complex due to their larger number and the more fragmented ownership structure. Still, there is a consensus in the international development community that strong coordination between MDBs would reinforce each institution's actions and increase efficiency. Operating in a more coordinated manner and working as a system allows MDBs to achieve better results. This is particularly important when tackling global public goods and addressing collective action problems like climate change. MDBs also help to scale up the mobilization of private financing for development.

MDBs can tackle debt distress associated with the COVID-19 pandemic in a coordinated fashion. So far, most of the debt relief initiatives have focused on the world's poorest countries, leaving aside most LAC countries. Collective MDBs actions to tackle debt problems in MICs are oriented toward expanding fiscal access and obtaining more financing from international markets at better rates. For example, by advocating for an MDB green sovereign debt guarantee scheme to help countries maintain market access and set the stage for a green recovery. Another option proposes that central banks, in coordination with the IMF and the MDBs, establish a special-purpose vehicle that would bridge the vast amount of currently available global liquidity and emerging economies' growing financing needs. The last suggestion consists of creating an off-balance-sheet vehicle purpose-built to take on more risk exclusively during a crisis, which multiple MDBs could access.

MDBs are uniquely prepared to address global and regional challenges of different nature at every stage of the economic cycle. The post-pandemic countries' demands will include the continuous requests for structural lending (i.e., the type of lending that was the original reason for creating the MDBs). MDB will also likely continue to fulfil an important catalytic role in crowding-in private finance for development. Countries' demands to MDBs will probably move in two other directions. On the one hand, it is expected that the demands for anticyclical financing be enhanced. On the other hand, countries facing debt problems will expect some help from MDBs. The size of MDBs responses will depend on the available spaces in their balance sheets and the ability to implement quick changes in their programming. MDBs will need an adequate capital level to maintain their relevance, a clear framework for counter-cyclical and contingent support to clients, and strong coordination among institutions.

In summary, the MDBs' future appears active. New viruses, environmental crises, and more economic shocks of a global scale make uncertainty a certainty for the future. Mitigating their most adverse effects will be a key task. The next decade may bring about a renewed role for multilateralism. The post-COVID19 world will be one of heavier governments, more public debt, and perhaps more regulation. For that, MDBs would need to continue changing to step up to the challenges. While important in the initial phases of a crisis, MDBs become critical in the recovery stage. Recovery financing should be deeply aligned with the Sustainable Development Goals.

I. Multilateral development banks in Latin America and the Caribbean: basic concepts and main institutions

There is a significant variation regarding MDBs ownership, funding sources, financial instruments, operations, and objectives. Despite the absence of a unique or consensual definition, some essential characteristics among these institutions can be highlighted (Xu, et al., 2019). First, MDBs need to have independent legal status. MDBs usually benefit from a special status governed by international treaties and are usually not subject to national regulations or local laws. Second, MDBs have a public-policy mandate. They are established to fulfill certain development or strategic objectives rather than maximize profits as commercial banks do. Third, in close relationship with the pursuit of public policy objectives, MDBs are established and supported by governments of two or more countries.[1]

The last common feature is that MDBs are self-sustainable financial institutions that leverage governments' capital support by taking on debt in international financial markets. As MDBs have neither deposits nor access to central bank funding, they heavily rely on market funding. MDBs issue bonds and securities purchased mainly by institutional investors (such as pension funds, commercial banks, insurance companies, and corporations worldwide) and governments. The funds obtained are used to finance medium to long-term finance to borrowing countries. In this way, countries in need of investments can use savings accumulated throughout the world.

The capital base of all MDBs includes the paid-in contributions and retained earnings. Paid-in capital represents the cash contributions made by government members during the successive replenishment of capital. Retained earnings are the net income that is held and added to the capital as accumulated reserves. MDBs usually maintain the full amount of their earning. This practice reinforces

[1] Overall, MDBs are part of a broader set of international organizations called international development finance institutions (DFI). MDBs are different from financial-stabilization funds like the International Monetary Fund (IMF), which are *international* but not *development* finance institutions. As opposed to national development banks, MDBs are established by governments of two or more countries.

MDBs' balance sheets significantly. Also, member countries grant MDBs a guarantee to repay their obligations if needed. This guarantee is called callable capital, and the member countries give it to MDBs to back up their bond issues. This portion of the capital subscriptions is subject to call only when required and up to the extent necessary to meet the MDBs' obligations with third parties on borrowings of funds or guarantees. To date, no MDB has ever had to draw on its callable capital.

Both borrowing and non-borrowing member countries make concessions to contribute to the strengths of MDBs' capital. The complex arrangement behind the institutional architecture of MDBs entails a mechanism for allocating these subsidies among borrowing member countries (Buiter & Fries, 2002). Shareholders do not receive dividends for their capital investments (i.e., net income is fully retained), nor do they charge any fees for the callable capital used as a guarantee. For donors, the multilateral nature of MDBs entrenches a comparative advantage in allocating finance for development by helping mitigate the risk of investing in developing countries by themselves (Rodrik, 1995). Borrowing members also make a distinctive contribution to MDBs by granting a *preferred creditor treatment* (PCT) on their exposures. The PCT implies that MDBs have priority in the repayment by allowing a senior claim to the borrowing members' reserves or primary government surpluses and are expected to be repaid even if the sovereign borrower restructures private or bilateral debt.

Altogether, these features assure that most MDBs enjoy high credit ratings, usually AAA or AA. As a result, MDBs generally access the international financial markets in more favourable financial terms than individual borrowing members. In turn, MDBs transfer their better funding conditions to their borrowing-country clients in the form of loans with long maturities and grace periods and low-interest rates. Clients demand loans from MDBs mainly because their financial terms are more favourable than what countries would get if they issued sovereign bonds or requested credits from commercial banks. Maintaining high ratings to obtain optimal and competitive financing to transfer to their clients is central to the MDBs' financial models. MDBs are particularly instrumental in channelling funds to developing countries when financial markets are thin. MDBs could be the major (if not the only) source of international financing for the smaller and less developed countries.

Most of the MDBs lend according to two main risk categories: with and without a sovereign guarantee. Sovereign guaranteed (SG) loans are those given to national governments (central or federal) and local governments or state-owned enterprises but guaranteed by the national ones. Most SG financing is provided on non-concessional terms. The pricing is based on the banks' cost of funding plus a spread that covers operative and administrative costs and accumulates capital. A typical non-concessional loan is charged at a LIBOR rate plus a spread that goes from 50 to 350 basis points, depending on the bank's credit rating and the loan's maturity. The fact that loans are classified as non-concessional does not preclude the possibility that they are cheaper than private lending, as mentioned in the previous paragraph.

Besides, many MDBs provide concessional SG lending to their poorest members. In the case of these concessional loans, the interest rates are subsidized and below market prices. A typical concessional loan can be repaid at a "bullet" (a single lump-sum payment at the bond's maturity) at 30 or 40 years, with a 0.25-0.5% yearly interest rate. In some MDBs, concessional loans can be provided from separates funds, which usually have different governance than the non-concessional window and their own administrative expenses. Moreover, borrowing countries receive non-reimbursable grants for technical cooperation programs. Grants can be financed by the MDB's financial resources or funds from donors administrated by the MDB.

MDBs provide financing without a sovereign guarantee (NSG) to private and state-owned companies and financial institutions. NSG loans can lend to a project (project finance) or a corporate structure (corporate finance). These loans should promote MDB's member countries' economic development by encouraging the private sector's expansion and modernization, complementing public sector financing. To do that, NSG lending aims at initiatives with high development impact, which often carry significant risks for which the private banking sector may lack appetite. The pricing of the NSG loans is set at market rates to avoid commercial banks' crowding-out. For some MDBs, the preparation, approval and administration of these loans are made by separate institutions with their own governance and administrative expenses.

Beyond financing, MDBs also offer a set of non-financial services. MDBs' lending comes bundled together with know-how and valuable experience gained in similar projects in other countries and is often complemented with non-reimbursable technical cooperation. While many of these components could be separately purchased by the client countries, they come all packed together in the case of the MDBs. The combination of financial, analytical, and technical support in one product (i.e., bundling) has proven to be highly valued by borrowers.

MDBs can be grouped by their regional coverage. There are global, regional, and sub-regional MDBs. Global MDBs lend to several continents. Regional MDBs (RMDBs) lend to just one continent Sub-regional MDBs focus on a specific region that is smaller than a continent. This classification is not absolute, as there are overlapping and border cases (Delikanli, et al., 2018).

MDBs' mandates and instruments have evolved along with the international community varying views on development. These mandates and instruments have also been continuously revised to accommodate their client countries' fluctuating needs as economic and financial market conditions shifted over time. MDBs' responses can be understood as the international community's answer to the challenges posed by critical situations at different points in time. In that regard, the COVID-19 pandemic is the latest crisis that motivates a strong and immediate response from the MDBs, but surely it will not be the last one. Box 1 briefly describes the evolution of mandates of MDBs since the creation of the first one in the post-second world war.

A. Major multilateral development banks serving the region

Several MDBs provide financing to Latin America and the Caribbean (LAC). The first global MDB, the World Bank, was established in 1944. At their conception, the World Bank was created to finance Europe and Japan's post-war reconstruction. However, once the Marshall Plan took over that duty, the institution focused on assisting poorer countries. The first loan for LAC was granted to Chile in 1953. In 1959, the Inter-American Development Bank (IDB) was created in the Cold War context, replicating the World Bank organization at the regional level. Since then, following a global trend of MDBs proliferation (Kellerman, 2019), MDBs have continued to be created. In LAC, the Central American Bank for Economic Integration (CABEI) was funded in 1960 and the Andean Development Corporation (CAF, now rebranded as Development Bank of Latin America) in 1970. Table 1 lists all the Multilateral Development Banks serving the region.

Table 1
Multilateral development banks serving Latin America and the Caribbean

Name	Acronym	Established
World Bank Group	WBG	1944
Inter-American Development Bank Group	IDB	1959
Central American Bank for Economic Integration	CABEI	1960
Development Bank of Latin America	CAF	1970
Caribbean Development Bank	CDB	1970
International Investment Bank	IIB	1970
Financial Fund for the Development of the River Plate Basin	FONPLATA	1974
Islamic Development Bank	IsDB	1974
OPEC Fund for International Development	OFID	1976
International Fund for Agricultural Development	IFAD	1977
Foreign Trade Bank of Latin America	BLADEX	1979
Nortth American Development Bank	NADB	1993
New Development Bank	NDB BRICS	2014
Asian Infrastructure Investment Bank[2]	AIIB	2016

Source: (Ocampo & Ortega, 2020).

The four largest MDBs account for more than 95% of development lending to LAC. They are quite different institutions in terms of geographic scope, assets, lending, capital volumes, and administrative size. Table 2 presents some basic information. The World Bank and the IDB are relatively complex organizations, with various sub-institutions and funds, each of these having its own membership, governing boards, and articles of agreement. At the World Bank, SG lending is provided by the International Bank for Reconstruction and Development (IBRD), the International Finance Corporation (IFC) provides NSG lending, and the International Development Agency (IDA) grants concessional loans. At the IDB Group, public sector loans are funded by its Ordinary Capital (ORC), and the IDB Invest provides NSG lending. Concessional loans at the IDB were traditionally granted through the Fund for Special Operations (FSO). In 2017, all the FSO's assets and liabilities were transferred to ORC. On the other hand, CAF and CABEI are simpler institutions, each with a single balance sheet for SG and NSG lending.

2 The AIIB was created to serve the Asia-Pacific region, but with the possibility of lending to members beyond Asia if the project delivers a clear benefit to the region. Currently, Brazil, Ecuador, and Uruguay are non-regional members, and five other LAC countries are prospective members. To date, the first project for LAC is being prepared: A $50 million credit line for Ecuador's National Financing Corporation.

Table 2
Main MDBs in LAC: basic information, 2019
(In million of dollars)

	World Bank Group			IDB Group		CAF	CABEI
	IBRD	IDA	IFC	IDB ORC	IDB Invest	SG+NSG	SG+NSG
	Non-Conc.	Concessional	NSG	SG	NSG		
Loans Outstanding	204 231	165 380	58 650	96 723	2 070	26 318	7 704
Of which LAC Region	61 757	2 925	12 085				
Commitments	27 976	30 365	11 135	12 961	4 668	13 010	2 638
Of which LAC Region	6 798	978	3 165				
Disbursements	20 238	21 179	10 518	10 574	1 607	10 043	1 934
Of which LAC Region	5 799	466	NA				
Total Assets	296 804	199 472	95 800	136 358		42 294	
Total Equity	40 387	168 171	25 182	33 871		12 797	
Paid-in Capital	18 034	241 343	19 567	11 852		9 370	
Callable Capital	269 968	…	…	164 901		1 590	
Net Income	-42	-1 114	-1 672	1 385		326	
Administrative Expenses	2 080	2 389	1 281	834		155	
Rating S&P			AAA	AAA		A+	

Source: Compiled by authors based on MDBs Information Statements.
Note: Data for the WBG refer to the fiscal year 2020 ended in June. For the rest, data correspond to the calendar year 2019. IDB ORC paid-in includes $5.8 billion from the transfer of FSO's assets and liabilities. CAF's paid-in includes amounts paid over the nominal value by shareholders. Data for IDB's ORC contain some NSG lending.

The four banks have different shareholding compositions. Non-borrowing countries dominate the World Bank's voting power, while CAF and CABEI are almost entirely owned by borrowing members. Borrowing countries have a slight majority (50.015%) at the IDB. However, the US is the biggest shareholder and enjoys veto power on major policy decisions that depend on the Board of Governors (the highest governance body of each MDB). Differences in shareholdings between borrowing and non-borrowing countries, together with who is the major shareholder, have a bearing on pricing and lending volumes (Humphrey & Michaelova, 2013), (Humphrey, 2014) and the pattern of capital accumulation, including the magnitude and frequency of capital replenishments (Artecona, et al., 2019).

Size-wise, the four MDBs are significantly different. The World Bank's total assets are 4, 14 and 51 times higher than those of the IDB, CAF and CABEI, respectively. World Bank's assets and outstanding (i.e., loans disbursed and not yet repaid) are allocated across six regions worldwide. The IDB is the main multilateral creditor of LAC in terms of outstanding. Its outstanding portfolio is almost four times that of the CAF and 30% above the World Bank's exposure to the region. In both the IBRD and IFC at the World Bank, LAC has the highest exposure among the six administrative regions (30% and 20%, respectively). However, the concessional fund of the Group (IDA) has limited exposure to LAC. Most of the countries in the region have already graduated from this fund. The IDB group is also the major institution in the region based on commitments (approvals) and disbursements, followed by CAF (in the last seven years).

The leverage of each institution varies with client diversification opportunities, the overall portfolio's risk, and the source of funds. With far more clients and hence stronger risk pooling prospects, the IBRD has the highest leverage. MDBs' leverage can be measured by the ratio of development assets (loan outstanding) to total equity. This ratio is 5 for the IBRD (5 dollars are lent per dollar of equity). In turn, the IDB has higher leverage than the other two regional banks because its geographical diversification is higher as well, and the risk embedded in its portfolio is lower. IDB's leverage is close to 3, while CAF's and CABEI's leverages are close to 2. IDA operates mainly as a fund, lending only its capital (with no leverage), and donor contribuitions funds its highly subsidized, long-tenured loans.

Box 1

The Evolution of Mandates of Multilateral Development Banks

MDBs views on development have continuously evolved. The World Bank's initial focus was on infrastructure, in line with the growth theories of the 1950s and 1960s that considered public infrastructure fundamental for development. By the early 1960s, development views had started to recognize human capital as a necessary complement to physical capital for economic development. The initial focus of the RMDBs broadening the scope beyond infrastructure to include social sectors (García, 2015). RMDBs also placed an important emphasis on integration.

The Debt Crisis in the 1980s dramatically changed the development priorities in the region. It revealed that sovereign borrowing from private banks exposed the region to a type of risk significantly different from that of borrowing from MDBs and other official sources. Private financing, if unrestrained, could make emerging markets more volatile, further deepening their economic cycles. Against this background, a structural reform process was undertaken in most countries in the region during the 1980s and early 1990s. The predominant view at the time, what came to be known as the Washington Consensus, was that developing countries needed to open their economies, reduce the scope of government intervention, and adopt prudent macro and monetary policies. In this context, MDBs promoted state-owned enterprises' privatization and addressed the states' scaling down and modernization.

To assist countries facing debt and balance of payment imbalances, MDBs developed a new set of tools, the "Policy Loans": an instrument for which money flowed to the treasuries of the countries in exchange for policy and institutional reforms that were thought to address the structural causes of the imbalances. The policy reforms were induced through the conditionality attached to disbursements. Policy loans would provide additional fast funding to heavily indebted countries in need of fresh funds. Inducing structural reform through policy conditionality required close coordination between the main international financial institutions to guarantee their implementation. Consequently, the roles of the IMF and Washington's established MDBs were coordinated to deliver on the implementation of those policy recommendations.

By the mid-1990s, the achievements of the Washington Consensus's reforms were deemed to have come short of expectations. Some of the reforms were later reversed. Following this change in paradigm, during the second half of the 1990s and the beginning of the twenty-first century, MDBs adopted a more complete and complex view of development. Efforts to substitute public sector financing and provision in social areas were re-evaluated, reassessing the role played by public sector institutions in achieving growth and development (Burki & Perry, 1998). This vision was anchored in Douglas North's "New Institutional Economics." This change resulted in project loans aimed at improving the public sector's efficiency and effectiveness, focusing on the quality of institutions in service delivery rather than reducing the size of the public sector.

Departing from the Washington Consensus, MDBs revised conditionality. Policy loans continued to be appreciated and demanded by client countries as a mechanism of budget support, but the conditionality included in those loans changed. The preparation of this kind of loans became more of a dialogue between the MDB and the borrower rather than an imposition. The twenty-first century also brought about new demands for social inclusion in the region that, together with the increased access to international financing enjoyed by most countries in Latin America, resulted in changes to MDBs operations. Interventions in poverty alleviation were strengthened, policy conditionality was reviewed, and governments' policy ownership was revalued. Environmental concerns continued to evolve while MDBs developed internal structures to address these issues and expanded their involvement with civil society to defend environmental and social safeguards.

Beyond SG lending, MDBs have always provided loans to the private sector. In 1956 the World Bank Group launched the IFC "to further economic development by encouraging the growth of productive private enterprise in member countries, particularly in the less developed areas, thus supplementing the activities of the IBRD" (IFC, 2017). Similarly, the IDB created the IIC in the early 1990s, although its ordinary capital always allowed NSG lending. Moreover, since its creation, CAF has provided financing with and without sovereign guarantees in similar amounts. The relevance of private-sector lending has significantly increased in the last 20 years. Policy changes worldwide placed a greater dependence on the private sector to promote development. Consequently, private sector lending and mobilization have been placed at the centre of MDBs strategies, increasing the demand for better coordination between the public and the private sector.

Finally, the New Development Agenda has imposed a re-focus of the mandates of the MDBs toward greater collaboration to achieve the Sustainable Development Goals (SDGs). As a result, MDBs current focus pays special attention to sustainability, social and environmental safeguards, climate change, and gender equality. According to this new mandate, MDBs should play a critical role in supporting their member countries' efforts to translate the SDGs into meaningful country-level targets, policies, programs, and projects. To fulfil this mission, direct and indirect financing (through mobilization) is required, as well as implementation support, policy advice, and technical assistance. Nowadays, the main strategic priorities and a substantial percentage of operations and financial flows in MDBs are associated with the SDGs. The New Development Agenda also calls for greater coordination among MDBs, including the convergence around core standards (Shanmugaratnam, 2018). Still, coordination has become progressively more complex over time due to the larger number of MDBs with significant differences in shareholding serving the region.

Source: Prepared by the authors on the basis of (Artecona, et al., 2019.

Only sovereign guaranteed windows of resources have access to callable capital, which, as we mentioned, is a guarantee granted by shareholders in case of impossibility of repaying MDBs' obligations. This callable capital is significantly higher in institutions with mixed ownership (borrowers and non-borrowers). The main value-added of the guarantees lies in those granted by the high-rated, non-borrowing member countries.

Banks also differ in how they use their income to accumulate reserves and increase equity. Net income is negative for the IBRD's and IFC's due, in part, to transfers to IDA. On the other hand, the IDB heavily relies on net income to accumulate equity, given the lack of appetite of IDB's shareholders for regular replenishments. Nowadays, only 35% of IDB's equity corresponds to paid-in contributions, meaning that accumulated reserves have generated 65% of the equity. CAF, which experienced four consecutive replenishments between 2007 and 2015, does not need to generate a large net income to increase its capital, as it relies on its members paid-in contribution. 73% of CAF's equity corresponds to paid-in.

Finally`, the more diversified the portfolio, the higher the donors' support, the clearer the policy mandate, and the better the capital adequacy, the higher the MDB's credit rating is. Capital adequacy refers to the amount of equity needed by an MDB to meet its financial obligations, given the risk embedded in its assets. The World Bank and the IDB are AAA institutions with a clear mandate from their Governors to maintain this rating. CAF and CABEI do not achieve the highest rating, in part, due to the limited diversification imposed by their sub-regional nature. Their ratings have been volatile, depending on the sub-regional economic context.

Having analysed the basic features and financial information of MDBs serving the region, the next section focuses on multilateral lending trends to LAC.

II. Stylized facts of multilateral lending to Latin America and The Caribbean

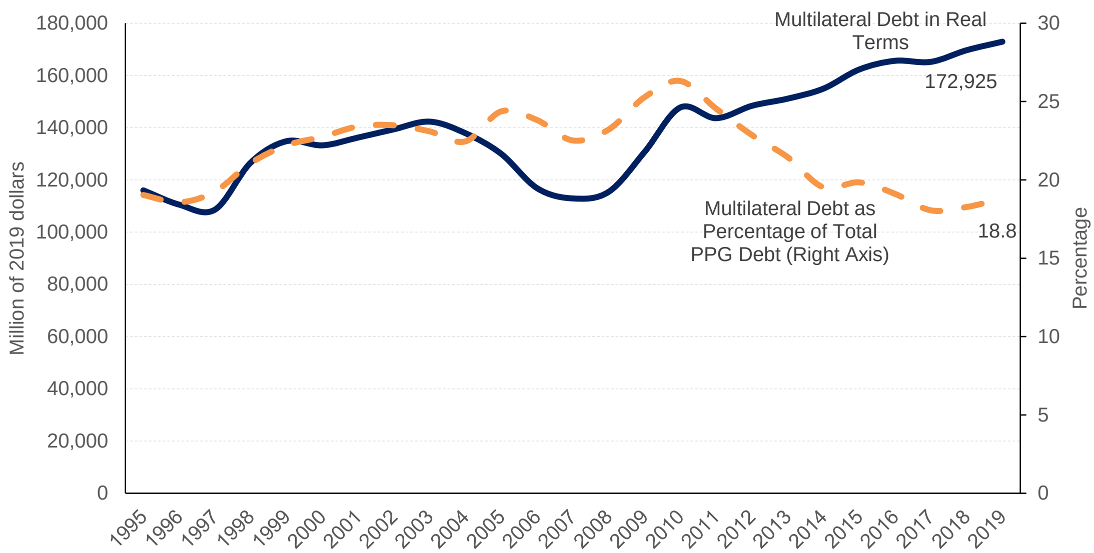
This section focuses on the basic trends of multilateral lending to the region in the last 25 years. These trends can be summarized as follows:

A. Multilateral debt has declined relative to total public debt during the last decade

Although multilateral debt has grown in real terms, it has been declining as a percentage of total external debt over the past fifteen years. The evolution of multilateral debt stocks has three well-defined phases. During the period 1997-2004, multilateral debt grew in the region. Many countries (notably Argentina, Brazil, Colombia, and Uruguay) obtained emergency loans to alleviate the emerging markets' crisis initiated in 1997 with the Asian financial crisis. Most of this debt (and particularly the emergency loans) was repaid during 2005-2008; in these years, multilateral debt shrank. The beginning of the GFC in 2008-2009 pushed multilateral debt up to $173 billion in 2019 (Figure 1). Multilateral debt grew 1.8% yearly in real terms during the 1995-2019 period.

There was a decoupling between multilateral and public and publicly guaranteed (PPG) debt during the last decade. PPG refers to debt either owed by the public sector or by the private sector but backed by public guarantees. Until the first decade of this century, both the ratio of multilateral to PPG debt and multilateral debt grew. Nevertheless, since 2010, while multilateral debt continued growing, the ratio of multilateral to PPG debt decreased by about 7.5 percentage points, from 26.3% to 18.8%. This decline resulted from a faster increase in public debt financed by private creditors (both through bonds and commercial banks) than multilateral debt.

Figure 1
Multilateral debt stocks in real term and as a percentage of PPG debt
(In million of 2019 Dollars and as a percentage)



Source: Compiled by authors based on International Debt Statistics and US Bureau of Labor Statistics.

PPG debt can be financed by official (multilateral and bilateral) and private creditors. The latter can be further divided into bonds and commercial banks' lending. Table 3 shows the composition of PPG debt among these categories. There is a prevalence of bonds over commercial banks' loans on the private creditors' side since the Brady Plan was launched in the early 1990s.[3] In the last 25 years, and especially in the aftermath of the GFC, international financial markets have opened to small countries and expanded to big ones, significantly increasing the region's capital flows. As a result, nowadays, 60% of the total public debt corresponds to bond issuances (more than $550 billion). Commercial banks' share lending recovered in the last ten years due to improvements in macroeconomic conditions in many countries and a low-interest-rate environment.

On the official side, the decrease of bilateral debt to LAC over the last two decades results from a concerted move of the international donor community to focus on Africa and away from middle-income countries (MICs), reducing the share of bilateral to only one-quarter of the 1990s'. On the other hand, multilateral debt increased its share up to 2010 and sharply decreased thereafter.

[3] Brady bonds were created to convert bank loans to Latin American countries into a variety of new tradable bonds after many of those countries defaulted on their debt in the 1980s.

Table 3
Public and publicly guaranteed debt by type of creditor
Latin America (excluding high-income countries):

	1990	2000	2010	2019
In percentage of total PPG debt				
Bonds	24.1	56	57	60.7
Banks + Other Private	38.8	9.6	8.8	15.6
Sub-total Private Creditors	62.9	65.7	65.9	76.4
Bilateral	19	11.6	7.8	4.8
Multilateral	18.1	22.8	26.3	18.8
Sub-total Official Creditors	37.1	34.3	34.1	23.6
In millions of dollars				
Total PPG Debt	309 989	394 997	478 778	919 000
Multilateral	56 034	89 863	125 977	172 925

Source: Compiled by authors based on International Debt Statistics.

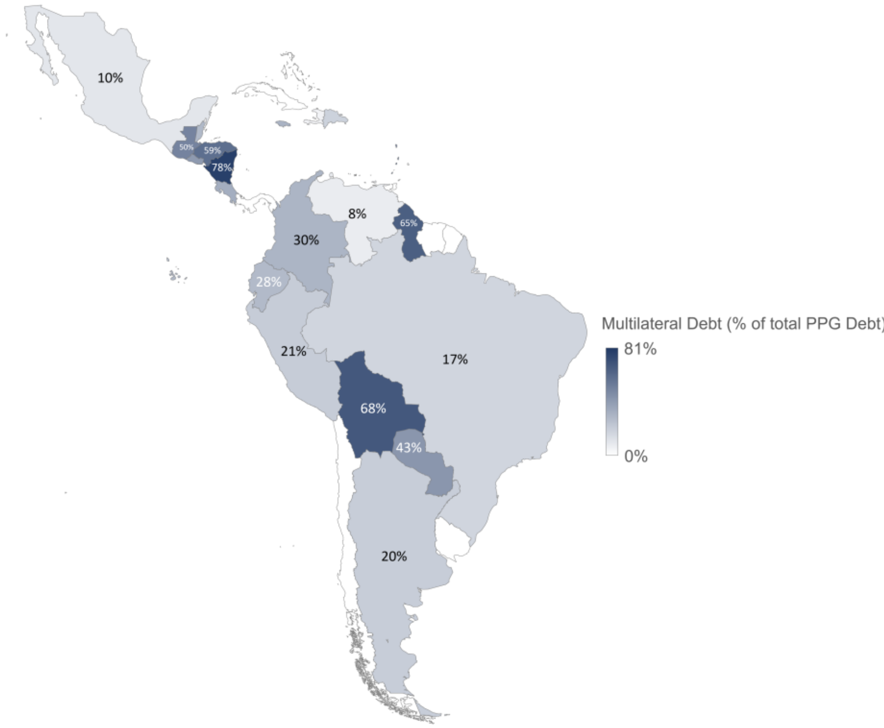
B. For the smaller and poorer countries, multilaterals remain the main source of public finance. Larger economies bear higher exposures to private and bilateral Chinese debt

Aggregated data underestimate the importance of multilateral financing in the smaller and poorer countries, where MDBs still account for more than half of PPG debt. Map 1 shows the percentage of PPG debt by country in 2019. The 18.8% figure in the previous table is a weighted (by debt size) average of bigger countries such as Brazil, Mexico, and Argentina (where multilateral debt is less than 20% of PPG); and smaller and poorer countries such as Bolivia, Guatemala, Guyana, Honduras, and Nicaragua, where more than 50% of PPG debt is multilateral. In these latter countries, international capital markets are still incipient, with fewer bond issuances and less private financing access.

Data on bilateral debt deserves to be handled with caution. The International Debt Statistics (IDS) may underestimate China's financing to the region. The reason is that Chinese loans could not be reflected in the previous figures, as the country is not part of the Development Assistant Committee (DAC) group of donors. New databases (Gallagher & Myers, 2020) look at the recent bilateral lending flows from China. Table 4 compares China's finance to Latin America with multilateral commitments during the period 2009-2019.

In those ten years, China, through its policy banks (China Development Bank and China Export-Import Bank), granted more than $131 billion to LAC governments and state-owned enterprises. More than 90% of these loans were allocated to four countries. In particular, in Venezuela and Ecuador, the amounts granted by Chinese policy banks were higher (in Venezuela, almost nine times, and for the biggest four countries, almost 30% more) than multilateral commitments during the same period. Overall, China's loans were equivalent to almost 60% of total commitments from MDBs to the region. Chinese lending piked in 2015-2016 and subsided after that. In fact, less than $10 billion have been approved in the last three years.

Map 1
Multilateral Debt as a Percentage of Total Public and Publicly Guaranteed Debt



Source: Compiled by authors based on International Debt Statistics.
Note: Excluding High-Income Countries.
The boundaries and names shown on this map do not imply official endorsement or acceptance by the United Nations.

Table 4
China's Finance to Latin America and Multilateral Commitments 2009-2019
(In millions of dollars and percentage of multilateral commitments)

Country	Loans from China	SG multilateral commitments	Percentage China/Multilateral (*percentages*)
Venezuela (Bolivarian Republic of)	58 200	6 713	867
Brazil	27 794	43 243	64
Ecuador	18 400	15 424	119
Argentina	17 070	29 958	57
Bolivia (Plurinational State of)	3 400	10 230	33
Jamaica	2 100	3 540	59
Subtotal	126 964	109 108	116
Rest of LAC	4 934	113 848	4
Total	131 898	222 956	59

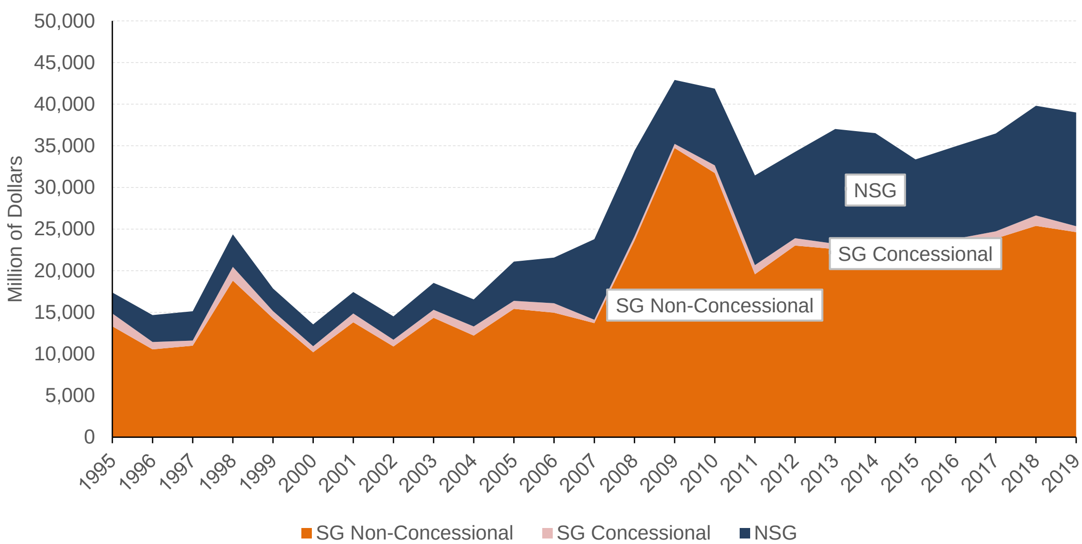
Source: Compiled by authors based on International Debt Statistics and (Gallagher & Myers, 2020).
Note: SG multilateral commitments correspond to PPG commitments to LAC, excluding high-income countries.

C. Multilateral non-sovereign guaranteed lending has increased faster than sovereign guaranteed, while concessional lending has fallen

The past decade has seen an increase in the role of NSG lending. By 2018-2019, lending to the private sector represented 35% of major MDBs lending to the region (more than $13 billion per year in approvals), compared to 20% in years 2004-2005 (Figure 2). This trend is consistent with the strategic focus on private-sector lending and mobilization to support the new development agenda and the Sustainable Development Goals (SDGs).[4] The rise of NSG lending highlights the importance of better coordination between the public and private sector windows.

Concessional approvals have declined steadily as a percentage of total lending. They now represent only 2% of MDBs approvals. Nowadays, most of the region comprises upper-middle and high-income countries (UMICs and HICs), while 20 years ago, it was of low and lower-middle-income ones (LICs and LMICs).[5] Most LAC countries have graduated from concessional borrowing, and very few still have access to concessional funding.

Figure 2
Total Approvals CABEI + CAF + IDB + World Bank, by type of risk and concessionality
(In millions of dollars)



Source: Compiled by authors based on MDBs annual reports.
Note: Data in calendar years except IFC from WBG with data in fiscal years.

[4] An example of the prime role that NSG lending has on MDB strategies is the cascade approach of the World Bank (WB, 2017). It states that projects should be financed with public funding only if there is no sustainable private sector solution. Policy regulatory gaps or weaknesses that hinder private financing shall be addressed before pursuing public funding.

[5] In 2014, 15 out of the 26 IDB's borrowing member countries were LICs or LMICs and 11 were UMICs or HICs. In 2020, only 5 countries are LICs or LMICs and 21 are UMICs or HICs.

D. Lending by regional banks has outpaced that of the World Bank to the region

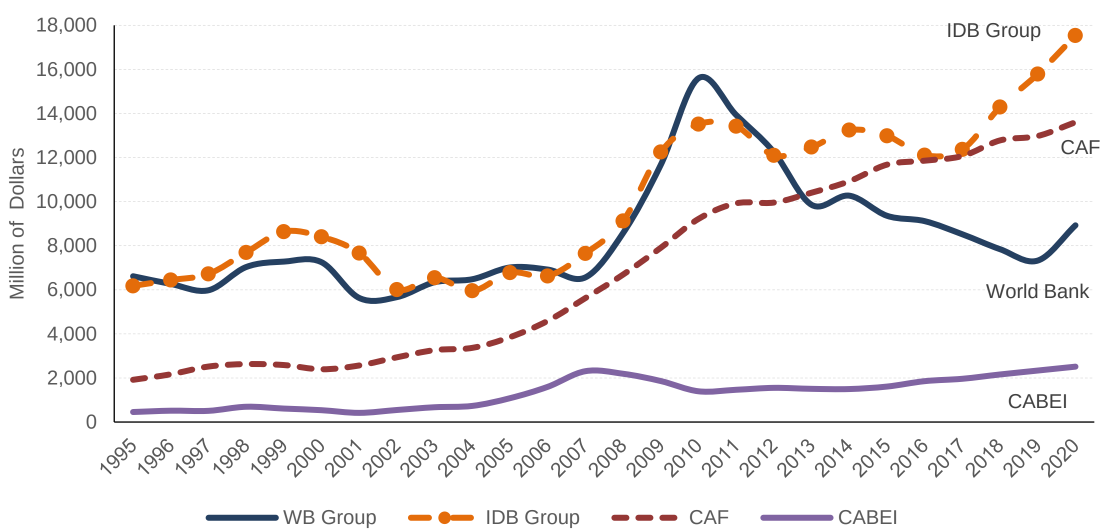
The continuous growth of CAF and the slowdown in World Bank lending in the last decade have led to a change in each institution's relative importance. Figure 3 shows total approvals (SG and NSG) to LAC by MDB. A 3-year moving average ended in each year is computed to moderate annual fluctuations. Roughly, on average, in the last three years, the IDB Group (IDB+IDB Invest) has approved some $17.5, CAF $13.5, the World Bank Group (IBRD+IDA+IFC) $9.0, and CABEI $2.5 billion per year.

The World Bank used to be the largest MDB (by approvals) in the early 1990s, representing 43% of total approvals by 1995. Its approvals to the region remained relatively constant until 2008. In the following three years (2008-2010), the World Bank, led by the IBRD, increased its lending to all regions, with LAC receiving more commitments than any other, reaching a historical maximum. After that, lending to LAC plummeted to pre-crisis levels as the institution focused on the world's poorest regions.

CAF, on the other hand, has experienced a sharp and steady increasing trend in approvals. Originally focused on the Andean region, in the 1990's CAF extended its membership to new Latin American members and Europe (Spain and Portugal), expanding its scope, capital, and lending capacity significantly. Since 2007 and propelled by successive capital increases, CAF doubled their approvals in the last ten years. By 2019, CAF approvals were 33% of total approvals to LAC, ranking as the second largest MDB serving the region.[6]

The IDB became the main source of development financing for LAC in the last decade. IDB's 2009-2010 lending significantly increased with respect to the first decade of this century. Once capitalized in 2010, its lending remained at levels similar to those during the critical years of the GFC. The capitalization of the private sector arm in 2015 allowed a further expansion. By 2019, the Group represented 41% of total approvals to the region.

Figure 3
SG+NSG Approvals by MDB to LAC, 3-year moving averages 1995-2020
(In millions of dollars)



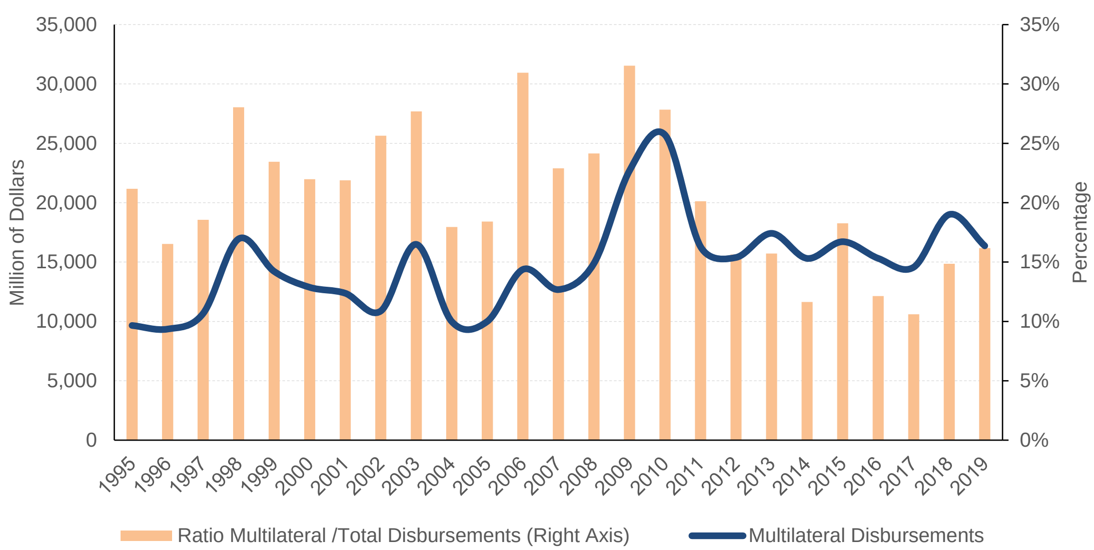
Source: Compiled by authors based on MDBs annual reports.
Note: Data in calendar years except IFC from WBG with data in fiscal years. Preliminary data for 2020.

6 Data of CAF approvals, however, have to be taken with caution as some of their disclosed approvals are indeed credit lines renewed every year.

E. Financial flows have been countercyclical, although cyclicality varies across multilaterals

During crises, when private lending to the region retrenches, MDBs' disbursements expand. This is consistent with the findings that government demand to MDBs is countercyclical while international government borrowing from private-sector lenders is procyclical, particularly in periods of limited global capital flows (Galindo & Panizza, 2018). Figure 4 shows how in every crisis (1997-1998, 2001-2002, and 2009-2010), MDBs disbursements peaked while post-crisis disbursements moderated, although average post-crisis disbursements remained above pre-crisis levels. While in non-crisis years, the share of MDBs to total disbursements is below 20%, during crises, this ratio usually surpasses 25-30%.

Figure 4
MDBs disbursements to Latin America
(In millions of dollars and percentage of total public and publicly guaranteed disbursements)



Source: Compiled by authors based on International Debt Statistics.
Note: Exclude High-Income Countries.

Cyclicality varies across MDBs. The countercyclicality of official lending is mostly driven by the World Bank's behaviour, while borrowing from RMDBs tends to be acyclical (Galindo & Panizza, 2018). Moreover, these authors find that official lending to LAC (as well as to East Asia) is more countercyclical than to other regions. As said, the World Bank's global nature allows it to manage its lending across regions stressing its anti-cyclical lending in the most affected regions. This is something RMDBs cannot do. IBRD approvals showed a clear inverted "V" pattern between 2008 and 2012, while the expansion size during the bust far exceeded that of the other institutions. Following the expansion, the IBRD implemented a post crises contraction similar in size to the previous expansion, which did not occur in either of the other institutions.

F. Multilaterals face a competitiveness problem regarding their highest-ranked borrowers

As client countries mature and become more creditworthy, the competitiveness of MDBs becomes a fundamental issue for the future of multilateral lending. Nowadays, several LAC countries have gained access to international financial markets at rates similar to those charged by MDBs. Figure 5 compares the sovereign yields with the all-in rate equivalents (i.e., including funding cost, loan charges and other fees) of the four main MDBs serving the region. Sovereign yields are computed by adding the Emerging Markets Bonds Index (EMBI) calculated by JP Morgan to the US 10-year Treasury Bill.

Price competitiveness is an important component of an MDB loan. MDBs' sovereign loans' financial conditions used to be far better than those of international markets for all clients. However, nowadays, these differential terms have narrowed in most cases and reversed in a few. MDBs are bureaucratic institutions that usually impose significant transaction costs on clients to prepare, execute, and monitor loans. Therefore, MDBs should be substantially cheaper than sovereign bond prices to attract demand. Otherwise, countries have large incentives to substitute multilateral for private creditors. In other words, long-term MDBs viability requires better credit ratings and lower funding costs than their clients.

As seen in Figure 5, nowadays, IDB's (currently the least expensive MDB in LAC) charges are similar to the sovereign yields of the best-ranked countries in the region (Chile, Panama, Peru, and Uruguay).[7] CAF and CABEI, two institutions with no AAA rating, charge higher prices on their loans, with loan rates above their best-ranked clients. On the other hand, all MDBs remain an excellent option to access external financing for countries with higher risk premiums.

To note, the IBRD has two different series, and none of them is a straight line, as the World Bank charges a premium for fixing the interest rate (30-50 basis point depending on the loan's maturity). Lines are not straight through countries because the World Bank has started setting increasing charges according to the borrower's income level. The difference between group A (recent IDA graduates) and D (high-income countries) is 5-65 basis points for a loan, depending on the loan's maturity. By price-discriminating against HICs and HMICs, the World Bank is progressively pricing-out some of these countries, a movement that can be seen as de-facto graduation. By moving away from HIC and HMIC, which make the majority of the countries of the region, the World Bank is progressively diminishing its relative exposure to LAC in favour of other regions, especially during non-crisis times.

While the World Bank has a graduation policy, RMDBs have not so far.[8] There is a rationale for RMDBs to lend to all their borrowing member countries, especially those less risky and with higher ratings because risk agencies tend to penalize both concentration and aggregate portfolio risk. As RMDBs are naturally concentrated, they need to keep on board all the possible clients. Moreover, increasing the exposure to less-risky countries reduces their overall risk exposure, which improves credit ratings. Because of these financial and risk considerations, it is difficult to foresee advances in the discussion on graduation at the RMDBs.'

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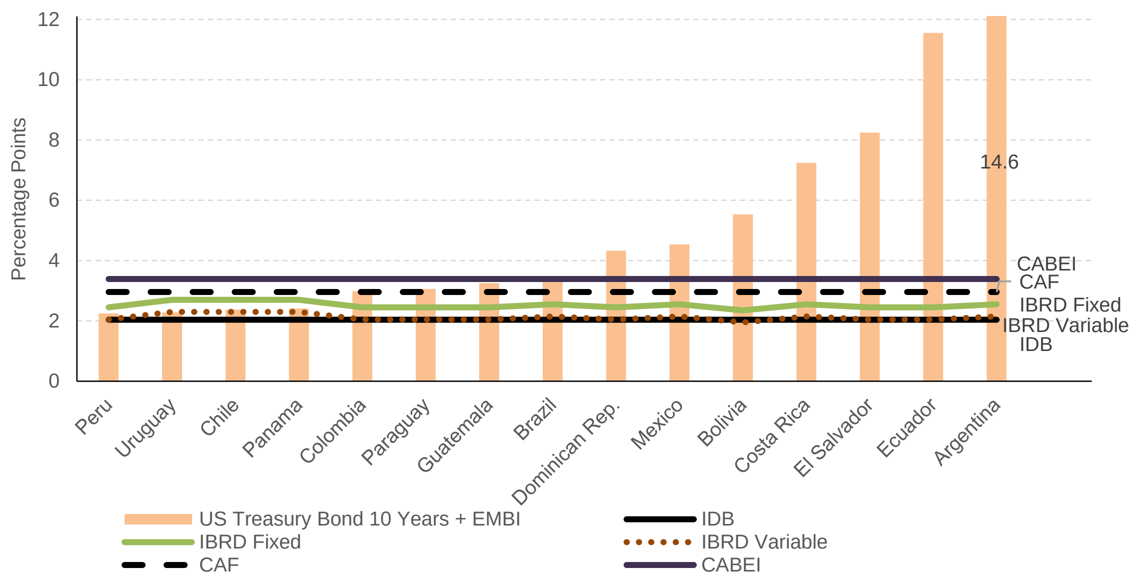
7 The government of Peru, for example, sold $4 billion of notes in November 2020, including securities coming due in 100 years with spreads of 170 basis points over US Treasuries. That marked the lowest-yielding century bonds ever sold by an emerging-market government. The bond sale came just days after Peru's President impeachment and deposition. Nevertheless, investors looked past the political noise.

8 According to IBRD policy, countries remain eligible to borrow until they are able to sustain long-term development programs without relying on bank financing. Thus, graduation is not an automatic consequence of passing an income threshold but is based on whether a country has reached a level of institutional development and capital-market access that enables it to sustain these programs. Under the World Bank's 2018 capital agreement, borrowing countries are expected to gradually reduce their portfolios once a base income threshold (the Graduation Discussion Income) is reached. The decision to graduate from IBRD involves a dialogue between the country and the bank and takes place on a case-by-case basis reflecting country context (Morris & Portelance, 2019).

Figure 5
Sovereign Yields and MDBs SG All-In Rate Equivalents
(In percentage points, EMBI data extracted on December 31, 2020)



Source: Compiled by authors based on JP Morgan and MDBs Finance Departments.
Note: The all-in rate is constructed as the sum of funding cost, lending spreads, and other fees in terms of spread. A 10-year swap for a 3-month Libor is used for computing the funding cost. IBRD fixed, and variable rates are for loans with a weighted average life of 12-15 years. Data for Argentina is capped to facilitate visual comparison.

Once the main empirical findings regarding multilateral lending to the region have been studied, the paper continues to analyse similitudes and differences between the multilateral response to this current COVID-19 crisis and the GFC of 2009-2010.

III. A tale of two crises: comparing the multilateral response during the COVID-19 pandemic and the global financial crisis

The COVID-19 is quite a different crisis than the GFC. Countries in LAC were better prepared in 2008 to cope with a crisis. At that time, they were at a different phase of their cycles, facing relatively high commodity prices with lower fiscal deficits and indebtedness levels. On the contrary, the ongoing shock caught the region amid a slowdown. Depicts the regional growth and external debt level as a percentage of Gross National Income (GNI) in the last two decades. Before 2009, the region had enjoyed five years of solid growth (above 4%). On the contrary, since 2014, LAC economies have had a lacklustre performance (especially the three biggest economies), growing on average below 1%.

On the fiscal side, the first decade of this century witnessed a reduction in external debt levels. After achieving a maximum following the Asian crisis at the beginning of the 2000s, the ratio of debt to GDP (or GNI) steadily decreased. Many countries embarked on a process of fiscal consolidation, establishing fiscal responsibility laws, medium-term fiscal frameworks, and fiscal rules (Pineda, et al., 2020). However, after some buoyant years, the region entered a period of low economic growth, falling commodity prices and persistent fiscal deficits. An environment of low-interest rates and easy access to international financial markets contributed to a sharp increase in the ratio of external debt to GDP. By 2019, this ratio was almost twice as high as ten years ago for the region as a whole. As a result, despite the fiscal efforts, the COVID-19 shock in the region is unfolding in the context of reduced fiscal spaces.

The GFC originated in the developed world and extended to the rest of the world at a slow pace than the COVID-19 crisis. In 2008, the recessionary effects of the crisis were more concentrated in the richest countries, and through them, they extended to the rest of the world by diminishing aggregate demand, altering expectations, and lowering available financing to the developed part of the world.[9] In contrast, nowadays, the world is witnessing an extremely fast economic retraction.

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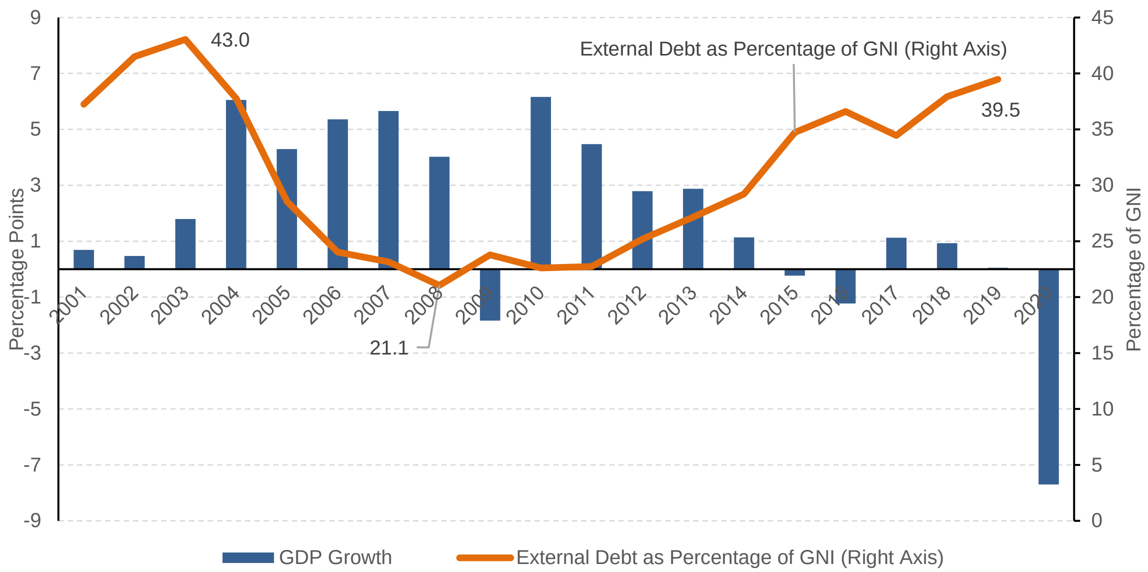
9 Ocampo (2020) argues that crisis should be called *North Atlantic* financial crisis because, although its effects were global, it concentrated in the United States and Western Europe. The bulk of emerging economies did not experience a financial crisis and their recovery was rapid, driven by China and high commodity prices.

Figure 6
Latin America, GDP Growth and External Debt as a Percentage of Gross National Income
(In percentage points and percentage of GNI)



Source: Compiled by authors based on CEPALSTAT and International Debt Statistics.
Note: External Debt as a percentage of GNI computed for Latin America excluding high-income countries.

The size of the policy interventions in the developed part of the world has shown a determination hardly ever observed before. To understand the magnitude of the response in the developed world, the US government has provided fiscal support approaching $3 trillion (some 14% of GDP), including over $1 trillion in loans to firms, direct transfers to households, and support to state and local governments (WB, 2020). This is equivalent to more than half of LAC's aggregate GDP ($5.7 trillion).[10] However, regional governments' economic support to firms and households has been significantly lower than in Europe, the US, or East Asia. Fiscal spaces have strongly conditioned packages' size in LAC. There is a negative correlation between the size of policies announced by countries and the level of their gross debt at the start of the pandemic. (Pineda, et al., 2020).

During the GFC, China's strong intervention helped emergent economies in LAC and elsewhere by stimulating demand and stabilizing commodity prices. On the other hand, the COVID-19 pandemic has triggered an international trade contraction and the disruption of global value chains. In addition, China's expansionary policies have been less pronounced than those adopted in the face of the GFC. It is worth noting that, as part of the collapse of the financial markets during the first phase of the crisis, there was a substantial capital outflow from emerging economies. However, the US Federal Reserve and other Central Banks' massive interventions managed to stabilize the financial markets. As part of this process, there has also been a recovery of private financing to emerging economies, propelled by the search for yield and the low-interest rates offered by developed economies.

[10] By the end of December 2020, the US Congress approved a new COVID-19 aid package for additional $900 billion. In total, the IMF estimates that fiscal and monetary packages to tackle the effects of the pandemic worldwide amount close to $12 trillion in fiscal measures and $7.5 trillion in monetary measures (IMF, 2020).

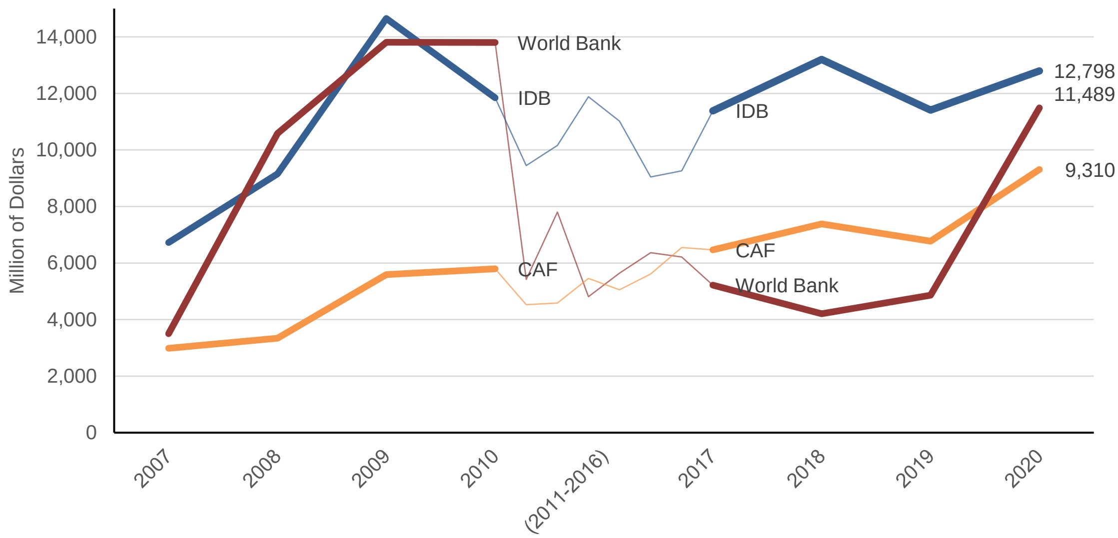
A. Multilateral response during the crises

Both crises triggered a strong multilateral response. MDBs complemented the liquidity provided by monetary institutions with long-term financing to support public spending and public and private investment by MDBs (Ocampo, 2020). All MDBs serving the region have proactively reacted to the pandemic's challenge and adopted special support measures: specific lines and facilities to address the crisis, streamlining of credit approvals, disbursements acceleration, and the option to reassess approved credits to use them for the emergency. In total, some $50 billion was approved this year by the four major MDBs. This represents an increase of 25% with respect to the previous year. To compare, in 2008, the first year of the GFC, the increase in lending reached 45%

While all MDBs increased approvals, their incremental response appears to be linked to their capital adequacy and portfolio-associated risks. The World Bank has so far presented the most drastic proposals regarding MDBs' incremental lending to LAC. On the other hand, the IDB and CAF have shown a relatively more limited incremental response. Even though these two institutions have taken important actions to support their borrowing member countries, their available additional resources to the public sector have been modest, given the crisis magnitude, the previous years' level of approvals, and the scale of the response during the GFC. Figure 7 shows approvals with a sovereign guarantee from the three institutions during 2006-2010 and 2016-2020.

Sovereign guaranteed World Bank's commitments (from IBRD and IDA) to the region more than doubled from the calendar year 2019 to 2020, reaching $11.5 billion. Although the World Bank's focus has shifted to the world's poorest countries (something that becomes evident when analysing the global increases in IDA vis-à-vis the IBRD), the resources provided to the region have increased significantly in 2020. In that way, the World Bank continues exhibiting a strong countercyclical behaviour in LAC. The World Bank also allowed the accelerated restructuring of projects in execution. It is still early to assess the overall magnitude of the World Bank response. As a benchmark, during the GFC, lending to LAC tripled from $3.2 in 2007 up to $10.5 billion in 2008, and then they continued increasing in 2009-2010 up to $14 billion.

Figure 7
CAF, IDB and World Bank, 2007-2010 & 2017-2020, Sovereign Guaranteed Approvals
(In millions of Dollars)



Source: Compiled by authors based on MDB's annual reports and project data information.
Note: Preliminary data for 2020.WBG is IBRD plus IDA.

The World Bank's anticyclical efforts can be better assessed when we focus on the entirety of its sovereign lending. The biggest increase in financing at the World Bank has taken place in IDA, the concessional window, which assists very few countries in the region.[11] This divergence could reflect strategic decisions within the institution to prioritize IDA countries to allocate resources (Duggan, et al., 2020). Overall, IDA commitments almost doubled between 2019 and 2020 (calendar years), from $18.5 to $33 billion. This increase compares to just 16% growth during the GFC. On the contrary, the IBRD commitments just increased by 14% to reach $26.6 billion in 2020, compared to a more than three-fold increase between 2007 and 2009. It seems that the World Bank is not only progressively concentrating in IDA countries but also aiming most of its anti-crisis power to these poorer countries too. For example, while IDA countries are making greater use of fast-disbursing budget support loans (Development Policy Operations, DPOs in World Bank's terminology), IBRD DPOs stayed essentially flat in Fiscal Year 2020 compared to 2019.

In 2020, The IDB approvals with sovereign guarantee were in line with its sustainable lending level. The sustainable level of lending (SLL) refers to the approval volume that allows an MDB to maximize its operability without jeopardizing its finances or requiring further capital replenishments. Approvals above the SLL (which at the IDB's is set around $12 billion per year) imply that in the future, *ceteris paribus*, the approvals' level must fall below the SLL to compensate for this excess. So far, deviations from the SLL have been moderate. The new resources approved to countries in 2020 were $12.8 billion, 12% above the previous year's level but below those approved in 2018. Of those, $8 billion were for operation explicitly focused on the pandemic's response, including financing for immediate public-health needs, safety nets for vulnerable populations, and support to fiscal measures to help

[11] Currently, Dominica, Grenada, Guyana, Haiti, Honduras, Nicaragua, St. Lucia and St. Vincent and the Grenadines have access to IDA resources.

mitigate economic impacts. This includes the request of five countries to access funds from the emergency program for macroeconomic and fiscal sustainability for $1.2 billion.[12]

The IDB implemented other operative measures to support their clients during this crisis. Anticyclical support centred on reformulating and fast-tracking operations, accelerating disbursements, and reorienting the pipeline through projects directly aimed to deal with the emergency caused by COVID-19. Government clients could redirect some of the resources previously allocated to projects in execution in other sectors to address the ongoing crisis. This has freed $1.35 billion in resources. The bank also expedited the execution of projects with large undisbursed amounts (including investment programs with slow implementation and programs with differed drawback options). It also approved a temporal increase in policy loans' limits (from 30 to 40% of total lending) to provide more fast-disbursing budget support to its borrowing members.

The IDB Invest (the Group's private arm) significantly expanded their lending envelope in 2020. In total, IDB Invest approved $6.7 billion, nearly doubling its 2019's total. On that, $3 billion corresponds to the Trade Finance Facilitation Program (TFFP), and the rest were loans for infrastructure and energy, corporates, and financial institutions.[13] Besides, the IDB Invest's account for approximately $2 billion in core mobilization. This concept refers to the volume of commitments made available due to an MDB direct involvement in mobilizing financing (for example, parallel loan participations and special funds administered) for which the bank charges administrative fees.

Most of CAF's support to governments has come in the form of credit lines and facilities. That means that not all funds approved are later actually disbursed. There was an important reallocation in 2020 from investment and policy loans towards credit lines and facilities. Most approvals ($4.1 billion) correspond to loans to provide countercyclical support to strengthen countries' fiscal management.[14] In total, CAF approved $8.9 billion until December 2020 with a sovereign and quasi-sovereign (state-owned enterprises and national development banks) guarantee. Like the IDB and the World Bank, CAF also allowed redirecting resources from projects in execution. Altogether, including the NSG support, CAF expects $14 billion in approvals for 2020.

The evolution of sovereign guaranteed lending between 2018 and 2020 is summarized in Table 5. Out of the three MDBs, the IBRD is the one with the greatest public-sector expansion to the region in 2020, both in absolute terms and the magnitude of the variation ($4.7 billion and 96%, respectively). This is not new. During the GFC, the World Bank was also the MDB with the highest expansion of lending to the region, both relative and absolute. Yet, the World Bank's total level of lending to the region in 2020 was still below that of the IDB.

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[12] These emergency loans belong to a special development lending category: a budget support lending instrument aimed at contributing to address the effects of a macroeconomic crisis on a country's economic and social progress. Conditions to access for this type of loans differ from standard projects. Moreover, loans are more expensive and have shorter tenures. In 2020, Costa Rica, Dominican Republic, El Salvador, Honduras, and Panama requested emergency loans.

[13] Under the TFFP, the IDB Group provides short-term loans to local banks to finance portfolios of eligible trade transactions and credit guarantees to global banks to mitigate any risk associated with trading instruments.

[14] In addition, $1.6 billion corresponds to a countercyclical facility for National Development Banks, $1.2 billion to a facility for countercyclical support to public utilities, and $350 million to a regional line of credit for extreme weather events, earthquakes, pollution, and epidemics.

Table 5
Sovereign Guaranteed Lending, 2018-2020, by MDB
(In millions of Dollars and percentage to the previous year)

	2018	2019	2020	Variation 2020/2019
World Bank	4 200	4 860	11 490	136%
IBRD	3 700	4 445	10 275	
IDA	500	415	1 215	
IDB	13 200	11 410	12 800	12%
Regular Lending Program	13 100	10 910	11 575	
Emergency	100	500	1 225	
CAF	7 365	6 740	9 310	38%
Loans	3 930	4 190	2 070	
Credit Lines and Facilities	3 435	2 550	7 240	

Source: Compiled by authors based on MDB's annual reports and project data information.
Note: Preliminary data for 2020. Can diverge for final figures that will be published in the annual reports. IDB includes ORC and Grant Facility.

CABEI approved $2.5 billion as part of a new strategy that projects $15 billion in approvals for 2020-2024. The bulk of these resources are channelled through a credit program to support Central Banks's liquidity management ($1 billion), sector public loans ($600 million), and a facility to provide loans, guarantees, and trade finance instruments to the financial sector ($350 million). In parallel, disbursements raised from $1.9 up to $2.3 billion. Away from its traditional focus on investment projects, CABEI created a policy loan instrument (called Operations of Policy Development) and approved $750 million through this credit instrument for El Salvador, Honduras, and Costa Rica in 2020.

Commitments only tell part of the whole story. The other part comes from the analysis of disbursements and, ideally, net flows to account for the fact that while receiving new resources, countries may be simultaneously repaying earlier loans. At the IBRD, disbursements in 2020 (calendar year) for LAC countries amounted to $8.76 billion, 85% higher than the $4.76 billion disbursed in 2019. At the IDB, SG disbursements increased by 50% to reach some $13.2 billion. Unfortunately, MDBs' do not report detailed information on disbursements or net flows as timely and disaggregated as in the case of approvals. The full information will be available only with the publications of the annual reports and financial statements. While somehow incomplete, the analysis of approvals still provides an accurate and up-to-date picture of MDB's engagement with the region.

On top of multilateral lending, the IMF has offered a significant response to the crises in terms of speed and financing size. The IMF's interventions have been particularly strong in LAC. Countries in the region have extensively used renewed emergency credit lines and flexible credit facilities. Between 2018 and 2020, the IMF has approved $185 billion in emergency financing. This is more than double the total SG commitments of MDBs during the same period. While the IMF's support to the region started before the COVID-19 outbreak, it had intensified in 2020. Out of $102 billion in financial assistance granted to 83 countries since the beginning of the crisis, the region (Western Hemisphere, in the IMF's organizational distribution) has received $64 billion. Table 6 shows the main programs approved by the IMF in the last three years.

Table 6
IMF's Financial Assistance to LAC, 2018-2020

Country	Type of Emergency Financing	Date of Approval	Amount (in millions of dollars)
Mexico	Flexible Credit Line	19-Nov	61 020
Argentina	Stand-By Agreement	18-Jun	55 749
Chile	Flexible Credit Line	20-May	23 930
Colombia	Flexible Credit Line (incl. augmentation)	May-20, Sep 20	16 948
Ecuador	Extended Fund Facility & Rapid Financing Instrument	Mar-19, May-20, 20-Sep	11 299
Peru	Flexible Credit Line	28-May-20	11 000
Other Countries			5 027
Total 2018-2020			184 973

Source: Compiled by the authors based on IMF.

Most of this financing is precautionary. The Flexible Credit Lines (FCL), approved by Chile, Colombia, Peru, and Mexico, is an instrument designed to meet the demand for crisis-prevention and crisis-mitigation lending for countries with very strong policy frameworks and track records in economic performance. It provides a valuable backstop and helps boost market confidence during periods of heightened risks.15 Beyond the Stand-By Agreement with Argentina and the Extended Fund Facility with Ecuador, fifteen countries have approved relatively smaller amounts of the Rapid Financing Instrument. This delivers rapid and low-access financial assistance to member countries facing an urgent balance of payments needs without requiring a full-fledged program in place. As part of the COVID-19-related rapid arrangements, borrowing countries have committed to undertake governance measures to promote accountable and transparent use of these resources.

B. A Brief History of Recent Capital Increases

While all institutions have expanded their credits to the region, the size of their respective responses appears to be linked to differences in capital adequacy and portfolio risks. The World Bank and BID-Invest, which have recently attained capital increases, presented significant reactions. So far, the IDB and CAF have proposed less impressive incremental responses. More than the amount, the priority has been to reassign resources to support the battle against the pandemic (Ocampo, 2020).

Therefore, it is important to analyse the evolution of equity in each institution. Figure 8 shows the equity in each MDB in 2007, the flows (paid-in contributions and accumulated earnings) between that year and 2019 (2020 for the World Bank, whose fiscal year closes in June), and the final equity position in 2019/2020. During this period, every bank processed at least one capital increase. When the GFC started, international financial institutions were encouraged by their major shareholders to boost the resources available through them substantially. Accordingly, global and regional MDBs dramatically expanded their lending beyond sustainable levels, running out of resources and obtaining a subsequent

[15] The FCL was created in 2009 as part of the process of reforming how the IMF lends money to countries. According to the Fund, the objective was to reduce the perceived stigma of borrowing from the IMF, and to encourage countries to ask for assistance before they face a full-blown crisis. Colombia, Mexico, and Poland were the three first countries to ask for this type of financing in 2009 during the GFC. Poland exited in 2017 and currently only Colombia, Chile, Mexico, and Peru are using these lines. None of the countries have so far drawn down on them.

capitalization (Weiss, 2011). Sub-regional MDBs also processed these discussions.[16] Notwithstanding, the magnitude, frequency, and rationale of capital increases have varied across institutions.

The World Bank approved two capital increases during this period for the IBRD and the IFC.[17] In 2010, the IBRD received its first capitalization in 20 years. It entailed a capital increase of $5.1 billion in paid-in and $81.1 billion in callable capital. With these contributions, total equity and capital expanded by 12% and 31%, respectively. On the other hand, IFC received a much modest capital increase of $200 million. For the IBRD, the package allowed a shifting in voting power in favour of developing and transition countries. Simultaneously, the World Bank agreed to sharpen its strategic focus.

The World Bank Group's shareholders subsequently endorsed in 2018 a package of measures that included a $13 billion paid-in capital increase ($7.5 for IBRD and $5.5 for IFC, significantly more balanced than the previous replenishment), and $52.6 billion callable capital increase for IBRD. The capital increase included general and selective tranches. The latter, to rebalance shareholding, reduce extreme under-representation and deliver an increased voice for emerging markets and developing economies. It also included a series of internal reforms and policy measures to strengthen the institution's operational model, effectiveness, and ability to scale up resources. The package followed through on shareholders' commitment to better assist all client countries in addressing global challenges while deploying scaled-up assistance to areas that most needed financing. Following, the combined financing arms of the World Bank Group are expected to reach an average annual lending capacity of nearly $100 billion between fiscal years 2019 and 2030.

Paid-in contributions allow the IBRD to offset accumulated losses and transfers to IDA. The losses in accumulated earnings (mainly explained by pension-related items) are significant, representing approximately 15% of IBRD's total equity. Paid-in contributions compensate for these losses. As a result, the level of equity by 2020 is almost identical to 13 years ago, before the GFC. To note, although the two capital increases involved $12.6 billion in paid-in, most of the contributions related to 2018's increase have not yet been made.

In 2010 the IDB's Board of Governors approved the 9th General Capital Increase (GCI9), adding $1.7 billion in paid-in and $68.3 billion in callable capital to reach a $170 billion capital base. Governors tied the capital increase to a series of reforms, emphasizing operational safeguards and oversight and adding a new income management model to regulate capital accumulation. Moreover, Governors voted $2 billion in grants for Haiti over 2010-2020 out of the bank's capital. In that way, grants to Haiti exceeded the total added paid-in. Later, in 2017, all the assets (and the few liabilities) of the concessional window (the FSO) were transferred to the Ordinary Capital to strengthen the capital base. For the ORC, this represented a significant increase in equity equivalent to $5.2 billion (more than three times the paid-in received in 2010). In the last ten years, the increase in lending associated with the GCI9 boosted operating income, reinforcing the accumulated earnings. By 2019, the total equity of the IDB was 66% higher than in 2007.

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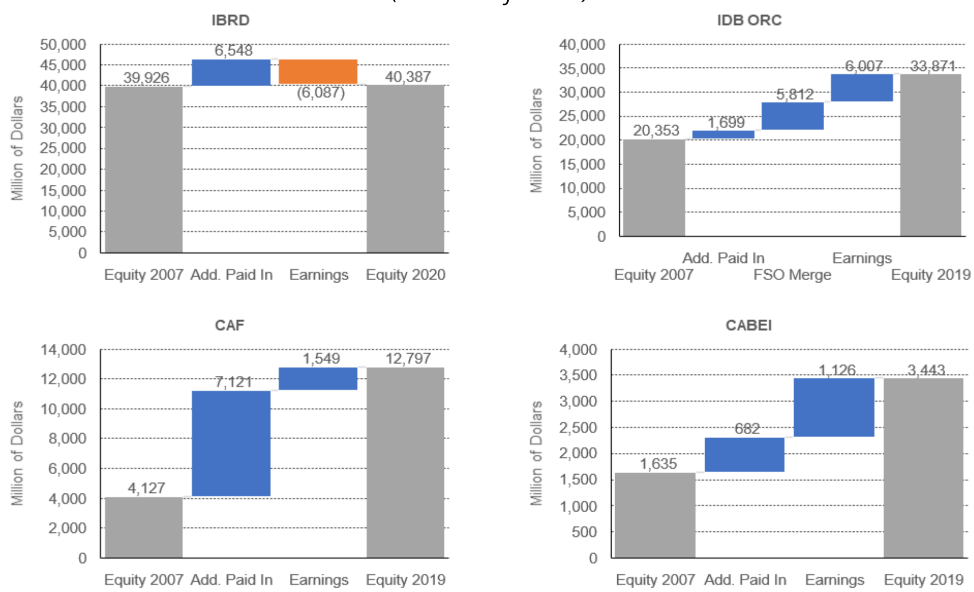
[16] Besides the four major institutions, other RMDB received capital increases during the period. The Caribbean Development Bank (CDB) approved in 2010 a capital increase of $1 billion, being the largest expansion of resources in the Bank's history. The Financial Fund for the Development of the River Plate Basin (FONPLATA) experienced a major process of institutional reform in the last ten years. Two capital increases were approved by the Board of Governors, one of US$ 1.15 billion in 2013, and with the second increase on 2016, the capital amounts to more than US$ 3 billion.

[17] As a concessional fund, IDA is funded largely by contributions from the governments of its richer member countries. Unlike other institutions where capitalizations are sporadic, IDA's partners meet every three years to replenish the fund. The most recent replenishment of IDA's resources, the ninetieth (IDA19), was finalized in December 2019, resulting in a $82 billion financing package for fiscal years 2021-2023, representing an increase of 3% in real terms compared to IDA18, which was discussed in 2016.

Figure 8
Equity Increases 2007-2019/2020 by MDB
(In millions of Dollars)



Source: Compiled by authors based on MDBs Information Statements.
Note: Data for the IBRD correspond to fiscal years ended in June of the corresponding year.

The Inter-American Investment Corporation (IIC) was capitalized and rebranded as IDB Invest in 2016, merging the IDB Group's private sector activities. The consolidation sought to enhance synergies and administrative efficiencies, as well as provide a single point of access to the full spectrum of products and services available to the private sector. Until then, these activities were conducted through separate windows.[18] The capitalization proposal included a $2 billion capital increase for the IIC, of which $1.3 billion consisted of new contributions by IIC member countries and $725 million of capital transfers from the IDB.[19] It is envisaged that after a transition period in which part of the NSG loans will be booked in the IDB's ORC, the IDB Invest will fund the NSG financing in its entirety.

CAF had four consecutive capital increases totalling $10.8 billion between 2007 and 2015. The absence of non-borrowing members and the prevailing favourable economic situation of the members in those years probably explain the amount and frequency of capitalizations. The authorized capital tripled to $15 billion, allowing the institution to expand its lending faster than other MDBs. As a result, CAF became the region's second source of multilateral financing. Most of this increase was in the form of paid-in capital. While at the IBRD and IDB, approximately $^{2}/_{3}$ of total equity corresponds to retained earnings, in CAF, the ratio of retained earnings to total equity is approximately $^{1}/_{4}$.

During this period, CABEI received two capital increases. The first one was approved in 2009 and implemented in 2012. It brought the total capital from $2 to $5 billion. In 2018, CABEI approved to increase the capital further, from $5 to $7 billion. The capitalization was implemented in 2020. The constitutive agreement was modified, and some countries increased their participation or became new members (Cuba

[18] The old IIC was a small institution with a separate governance structure in charge of fostering private sector development, focusing on lending to regional banks and small and medium-sized enterprises. The IDB's ORC uses to fund large private-sector loans.
[19] The US, who had 23% of shareholding at the IIC refused to participate and diluted down to the 16%. The dilution was cushioned by the transfers from the IDB, where the US have 30% of shareholding.

and South Korea). CABEI has consolidated as the MDB with the most relevant presence in the Central American sub-region, with participation close to 50% in the region's disbursements in the last 15 years.

In summary, since 2016, the IBRD, IFC, IDB invest, and CABEI have obtained capital increases, and IDA received a substantial replenishment. These capitalizations allowed each of these institutions to significantly increase their finance to the region in 2020. The last capital increase for CAF was negotiated in 2015, and it is still receiving contributions. On the other hand, the last capital increase at the IDB occurred further back in time. The new IDB's president (elected in October 2020) has launched a discussion to increase the capital and expand the annual lending capacity to $20 billion a year. At the IDB and CAF, their equity level and the portfolio-associated risk could condition a further expansion in lending. The next subsection analyses how the level of capital and the risk embedded in portfolios can affect MDBs' lending levels via CRAs' assessments.

C. Credit Rating Agencies and Multilateral Development Bank's Operative

Maintaining high ratings to obtain optimal financial terms to transfer to their clients is key to the MDBs' financial models. Consequently, to preserve the highest possible rating is a clear policy mandate of these institutions. The CRAs' periodic surveillance on MDBs' financial and business profiles influence MDBs' operations (Humphrey, 2017). This section focuses on how rating considerations constraint MDBs lending, especially during a crisis. To complement, Box 2 briefly describes S&P's methodology to evaluate MDBs. S&P is the world's largest credit rating agency. Its methodology to evaluate MDBs is arguably the most transparent and easiest to replicate.

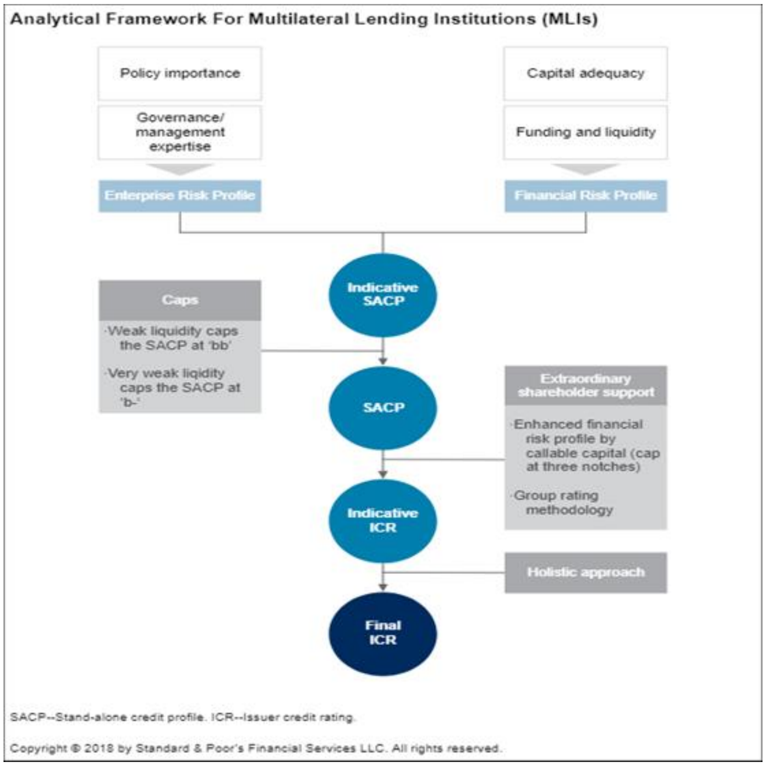
As discussed in Section II, MDBs disbursements show a countercyclical pattern. Sovereign demands from member countries tend to increase during recessions and moderate during peaks. Countries' financial needs are countercyclical in nature, and alternative financing sources become more expensive and tend to dry out during busts. As cyclical behaviours are usually correlated among clients, MDBs typically face a higher demand during a crisis.

On the other hand, the CRAs' models to evaluate MDBs are highly procyclical. Procyclicality in these models comes from the fact that CRAs compute asset risks at a point in time rather than over the cycle. Outstanding portfolios become riskier during a crisis. Many country ratings are downgraded in those times. Consequently, the value of risk-weighted assets increases and the ratio of equity to RWA (risk-adjusted assets to capital, RAC) is reduced. As a result, MDBs ability to leverage their lending is tightened. Theoretically, MDBs have the financial firepower to help developing countries deal with the impacts of crises like the Covid-19 (Humphrey, 2020). However, a significant expansion of lending without an adequate level of capital to compensate for the extra risk embedded in the new loans and the overall portfolio risks can trigger a downgrade. In this way, CRAs might limit MDBs financing expansion during crises and hinder MDBs anticyclical lending. The CRAs methodologies, which adapt methodologies designed to assess commercial banks, fail to capture the anticyclical role embedded in MDBs. They could incorporate cycles as a key component of the business model of MDBs and, as such, could look into the entirety of the cycle to assess capital sufficiency.[20]

[20] Methodologies for adjusting the effect of the cycles do exist; they are frequently used in public finances for the calculation of the budget deficits. The "structural deficit" adjusts the observed total budget deficit for the effects of the cycle. The observed deficit is then the sum of the structural deficit and the cyclical deficit (or surplus). These methodologies could inspire the computation of a "structural rating" that, while controlling for the effect of the cycle on the portfolio, would incorporate a key mandate of the MDBs: mitigate the effects of the cycles in their client countries.

Box 2
Standard and Poor's Methodology to Evaluate Multilaterals

S&P framework to analyse MDBs consist of different stages. First, it evaluates the enterprise risk and financial risk of an MDB. This is the basis to determine the Stand-Alone Credit Profile (SACP). Weak liquidity could cap the SACP at a low rating. After, the final Issuer Credit Rating (ICR) is reached by incorporating any extraordinary shareholder support and considering a holistic approach. The following figure depicts the analytical framework.



Because CRAs are primarily interested in the issuer's creditworthiness, a central element of the analysis is the capital adequacy, meaning how much capital is needed to meet MDBs financial obligation given the risk embedded in their assets. S&P determines the capital adequacy of MDBs in two steps: the first step assesses the MDB's capital and assets according to the risk-adjusted capital (RAC) ratio. This ratio is the cornerstone of the capital adequacy analysis. It evaluates the degree to which an MDB's capital would cover losses that could arise following a scenario of financial stress in the borrowing member countries. The RAC ratio compares an MDB's capital to its risk-weighted assets (RWAs). To ensure comparability, the methodology to determine the RWAs is identical to the one used for commercial banks. RWAs are computed applying specified risk weights to the various exposures.

The second step adjusts to reflect the specificities of MDBs. S&P adjusts the risk weights to reflect MDBs' preferred creditor treatment and their portfolio concentration. Because of the PCT, MDBs have a lower default probability and higher recovery expectations on their exposures than commercial banks. S&P also adjusts for concentration and diversification. This adjustment is called single-name concentration. It controls for the fact that the MDB's portfolio of clients is much smaller than that of commercial banks. Given that many MDB's are concentrated on a few sovereigns, the single-name concentration adjustment for sovereign exposures is substantial, leading to a reduction of the RAC ratio in most cases. An adjusted RAC ratio above 23% is considered extremely strong, meaning that it is almost sure that an MDB has enough capital to face a scenario of severe distress on their borrowing members and still meet all its financial obligations.

The next step is to evaluate MDBs funding and liquidity. How an MDB funds its business directly affects its ability to maintain lending volumes and to meet obligations. Funding is evaluated positively if the MDB has established market access that substantially exceeds its liquidity needs. Liquidity analysis centres on an MDB's ability to manage its liquidity needs over extended periods, even under adverse market and economic conditions. Both the capital adequacy and the funding and liquidity determine the financial risk profile of the institution. This financial risk can be categorized from extremely strong to very weak.

The financial risk profile is combined with the enterprise risk profile to determine the SACP. The enterprise profile blends the assessment of an MDB's policy importance and its governance and management expertise. Three main factors inform the view of an MDB's policy importance: the role and the public policy mandate; the strength and stability of the relationship with the shareholders; and the PCT. The latter is evaluated by computing the arrears that an MDB has had in the last ten years as a proportion of total outstanding. The analysis of governance and management expertise is mostly qualitative and based on MDB's public mission.

Once the assessment of the SACP is complete, the framework evaluates the likelihood that an institution would receive extraordinary shareholder support to service its debt obligations if needed. For MDBs, extraordinary shareholder support usually comes in the form of an injection of callable capital, which is a commitment by each shareholder to make additional capital available when necessary to avoid an MDB's default on borrowing or a call of a guarantee. S&P reflects the positive impact of the callable capital on the MDB's creditworthiness by assessing how callable capital would affect the RAC ratios. The final MDB credit rating (the ICR) is the combination of the "enhanced" financial profile (including the benefit of the callable capital) and the business profile.

Source: Prepared by the authors on the basis of (S&P, 2020). The original methodology was published in 2018.

CRAs penalize portfolio concentration. Adjustments in this regard (called single-name concentration) can create substantial changes in CRAs' assessment. Especially if the outstanding loan balance is concentrated in relatively riskier countries, increasing the overall credit risk. Concentration risk needs to be evaluated both on an individual borrowing country basis and taking into account the correlation among countries affected by a common event. Single-name concentration is particularly relevant for RMDBs. Considering the regional nature of their operations and the relative sizes of their clients' economies, RMDBs are expected to have a concentrated portfolio. At the IDB and CAF, the five largest exposures account for almost 2/3 of the outstanding loan balance. At the IBRD, the five largest borrowers (including two from LAC) account for 40% of the exposure.[21]

Risk considerations and CRAs views also matter for debt standstill discussions. The World Bank declined to participate in the debt service suspension initiative (DSSI) announced by the G20 in April of 2020 because doing so would endanger its credit rating and thus its ability to lend to low-income countries in the future (Duggan, et al., 2020). The DSSI offers suspension of payments (both principal and interest) on loans from official bilateral creditors to 73 low-income countries. Only the eight IDA countries are eligible for the DSSI. The balance sheets of the MDBs' non-concessional windows would be severely affected by debt forgiveness due to the impact of this kind of initiative on the PCT and MDB's financial results and portfolio performance. Every debt forgiveness in multilaterals has happened only in the non-concessional window of resources so far, where donors can replenish the funds and compensate for the losses incurred. As a middle-income region, LAC should find other alternatives to the debt problem that will probably emerge in the aftermath of this crisis.

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[21] The five largest borrowers for the IDB are Mexico, Brazil, Argentina, Colombia, and Ecuador. At the IBRD, the five largest borrowers are India, Indonesia, China, Brazil, and Mexico. At CAF, they are Argentina, Ecuador, Venezuela, Colombia, and Bolivia. CAF's substantial exposure to Argentina, Ecuador, and especially Venezuela jeopardizes its credit rating. In 2020, CAF's (which has experienced payment delays from Venezuela since 2017) approved a program that allows the repurchasing of Venezuela's shares to pay down its debt coming due from the sovereign. At that moment, S&P revised CAF's outlook to stable from negative. (S&P, 2020). On 2018 Venezuela entered into nonaccrual status with IDB as well, with a total loan balance of US$2.01 billion.

IV. The renewed role of multilateral development banks: key issues

MDBs have played a pivotal role in the advancement of LAC, and they continue to face increasing demands from the region. These demands have been shifting in content over time while expanding in terms of volume. Beyond the permanent needs, governments recur to the MDBs for their financing and advice every time the region confronts a negative shock. The ongoing pandemic has reinforced this MDBs' role in crisis mitigation. MDBs that serve the region have increased their lending and are decisively contributing to the governments' efforts to handle the sanitary aspects and the social and economic impacts of the COVID-19 crisis.

MDBs will likely remain relevant partners in development in the long run because they are uniquely prepared to address global and regional challenges of different nature at every stage of the economic cycle. While important in the initial phases of a crisis, MDBs become critical in the recovery stage. Beyond immediate public health response, recovery financing should be deeply aligned with the SDGs. Particularly in poverty reduction, gender and diversity, income inequality, and climate change mitigation and adaptation support. MDB should also continue to fulfill an important catalytic role in crowding-in private finance for development.

The post-pandemic countries' demands will include the continuous requests for structural lending, i.e., the type of lending that was the original reason for creating the MDBs. This includes upgrading inadequate infrastructures, addressing social needs, and improving existing institutional frameworks. Moreover, the future of these institutions will be progressively connected with the provision of global and regional public goods, including investments for adaptation and mitigation to climate change, the combat of infectious diseases, and the support for dealing with economic migration. The post-pandemic will likely move countries' demands to MDBs in two other directions. On the one hand, it is expected that the demands for anticyclical financing be enhanced. On the other hand, countries facing debt problems will expect some help from MDBs. This includes, for the few remaining lower-income countries in LAC, debt forgiveness initiatives.

The effectiveness and efficiency of the MDBs in the medium term will likely depend on their successful adaptation to the new circumstances. For that to happen, changes in their governance may be necessary to make these institutions more flexible and cut down on waste and improve efficiency. The institutional framework for the governance of the MDBs working in LAC was set up more than half a century ago. These institutions may need to modernize key aspects of their institutional structure. Newly set up institutions such as the AIIB, and the NDB-BRICS have designed more agile governance structures. However, for long-time established MDBs, reforming their articles of agreement usually requires parliamentary ratification by all their member countries, making the process extremely difficult.

MDBs will need both *muscle* and *coordination*. To respond effectively, they need to be prepared both individually and collectively. These institutions need to have the financial power and capital adequacy to deliver a sizable response during the crisis and articulate a coordinated response to the region's needs. Regardless of the recovery's speed and shape, the post crises will leave governments more stressed out from a fiscal point of view. They will likely face more acute indebtedness problems, which, in turn, will trigger new demands.

In summary, the post-pandemic may bring about a renewed role for multilateralism. For that, MDBs would need to continue changing to continue supporting fundamental challenges like economic growth, poverty reduction, and the implementation of SDGs in the region. Based on the findings of the previous sections, we analyze three main issues that, in our opinion, will be key in determining how MDBs could adapt to the new circumstances and expand their financing available to both the public and private sectors: Providing anti-cyclical support, maintaining an adequate level of capital, and encouraging strong coordination among MDBs.

A. Anti-Cyclical Support

The COVID-19 pandemic reinforced the idea that MDBs play a key role in mitigating negative shocks. Once confronted with a crisis (especially one of this magnitude), the governments of developing countries and emerging economies face unusual demands from their citizens. At the same time, they have restrictions to access the international financial markets. In those moments, MDBs are critical to helping alleviate the crisis. This role neither erodes the discipline within the international financial architecture nor creates incentives towards fiscal mismanagement in recipient countries (Avellán, et al., 2018).

Most of the countries in the region increased their lending from MDBs in 2020. This included the rise in the amounts for budget-support loans, the use of lines of credits, and the request for emergency loans. MDBs also speeded up their disbursements and allowed projects' reallocation toward critical necessities. As a result, MDBs have significantly contributed to the first response to the crisis. Furthermore, 21 LAC countries recurred to the IMF for financial assistance, especially for precautionary support.

MDBs financial models are not always adequately structured to respond to cycles. Multilateral sovereign lending tends to follow government expenditure, which is pro-cyclical by nature (Avellán, et al., 2020). An institution's capability to behave countercyclically and expand activities during a descending phase of a cycle is linked to its ability to contract its approvals and lending during the ascending phase. Managing cyclical lending is a difficult task, and it could require changes in governance, to develop the ability to modify lending rapidly. Shareholders need to clarify how they want MDBs to approach cycles. Whether they want to reserve a space exclusively for being used during crises (refraining from some project opportunities during the cycle's upswing to guarantee lending space during the rainy days); or routinely approve programming exercises that allocate the maximum possible every year, irrespective of the cycle stage. Addressing cycles should include designing specific products with different pricing and cycle-appropriate repayment periods, likely to be shorter than the standard 20-25-year repayment of regular loans.

Beyond expanding or contracting the level of resources allocated each year, an important element of MDB's anti-cyclical support is the possibility of offering ex-ante financial support to face crises. While the MDBs have traditionally focused on ex-post emergency lending, they have progressively extended the set of contingent and precautionary loans. Ex-ante instruments are meant to guarantee the availability of funds in anticipation of financing needs. Disbursements can be at the sole request of the borrower or conditional on the occurrence of a certain state or event (financial crises, external shocks, natural disasters, and health-related incidents).

MDBs count with precautionary instruments: Loans with differed drawback options (DDO). Like the IMF's FCL, these budget-support loans are approved (under the same conditions that a regular policy loan) but not immediately disbursed. Besides this precautionary lending, which is disbursed at the client's request, MDBs also offer catastrophe-based contingent funds, which become available for disbursement after a drawdown trigger is met (typically the country's declaration of a state of emergency). This type of loan usually allows for a reallocation of funds from previous projects. The amount to be disbursed is generally a function of the event's intensity and the population affected.

Contingent and precautionary instruments involve significant benefits to borrowing member countries.[22] They provide potential signaling effects, more certainty of quick disbursement of funds, and better liquidity management. However, most countries have not been willing to pay a premium over regular lending terms for contingent instruments, especially standby fees, which must be paid before a crisis occurs (OVE, 2016). Other downsides sometimes include unclear eligibility criteria, uncertainty regarding the availability of funds, lesser use of the annual envelope, and limited knowledge of these tools. MDBs should continue discussing clients' needs and preferences for these instruments, as they have proven their potential to be key elements of anticyclical support.

Outside specific emergency lending, which is more expensive and used only as a last resort by clients, policy loans are a mechanism for MDBs to respond to crises quickly. UMICs with relatively strong internal capacity value policy loans because this type of loan provides borrowing member countries with flexible, liquid, and fungible funding to support policy reforms. They are also cheaper to prepare and monitor, involving fewer safeguards and transactional costs than investment loans. However, non-borrowing member countries are generally reluctant to expand policy loans as they doubt their development potential due to their decreasing conditionality over the years. The discussions about the limits of budgetary support lending and the prioritization of faster disbursement over conditionality will probably intensify in the near future. The adequate mix of instruments is also part of a wider discussion on offering UMICs and HICs more appropriate financing instruments to increase MDBs competitiveness and demand from these countries.[23]

CRAs limit MDBs' countercyclicality. Achieving the highest possible rating is a key mandate for MDBs. Because of that, MDBs´ finance departments take a conservative approach to their capital adequacy, inducing MDBs to keep low leverages. MDBs' equity to loan ratios vary from 20 to 60%, compared to 10-15% for most commercial banks (Humphrey, 2020). During crises, risk-weighted assets (including the outstanding portfolio) rise. To control for that and maintain a strong risk-adjusted capital ratio, MDBs should either accumulate capital (for example, by increasing loan charges) or restrain lending. This conservative approach and the utmost importance that MDBs put in preserving their AAA are often criticized due to the fairly modest reduction in funding cost (compared to AA+). They argue

[22] Uruguay is a good example of the DDO's benefits. Since 2009, the country approved (and renewed) DDOs and lines of credits with CAF, IDB, and the WB for almost $3 billion. In 2015-2016 CRAs valued these lines to maintain Uruguay's investment grade amid regional downgrades for Argentina and Brazil. Between March and April 2020, at the Outbreak of the COVID-19, Uruguay could quickly disburse $1.5 billion from multilaterals to cushion the immediate fiscal impact of the crisis.

[23] For example, for countries with robust systems like Chile, it has been suggested to go beyond policy loans and explore a strategy for directly financing budget lines under government programs. This option would require the incorporation of a "certification" process for the technical and fiduciary aspects of government programs (OVE, 2018).

that MDBs can appreciably leverage their resources and ramp up their lending during crises if they are able to risk their AAA (Settimo, 2019), (Humphrey, 2020), (Munir & Gallagher, 20202).

With clear financial policies (including the management of cycles) and dialogue with CRAs, maintaining the highest ratings and expanding lending during crises should not be incompatible. MDBs can overcome the procyclical nature of CRAs' models as long as they develop the discipline to reserve capital and lending space and build substantial buffers during expansions. Of course, buffers should be constructed to be used during crises and not to over-guarantee ratings even under extremely unlikely scenarios. On the other hand, CRAs should continue reviewing their methodology (originally designed for commercial banks and adapted for MDBs) to acknowledge the utterly unique nature of MDBs, particularly regarding their highly conservative treatment of single-name concentration risk and insufficient allowance for preferred creditor status (Perraudin, et al., 2016). S&P has already made progress in that direction.[24]

B. Adequate Level of Capital

Shocks response requires well-capitalized institutions. The pandemic has highlighted the importance of having MDBs well prepared to confront the current and upcoming crises. The response to the exceptional demands generated by the COVID-19 crisis is stretching the balance sheets of the MDBs, especially the regional ones. As the size of MDBs' response is linked to the available spaces in their balance sheets and their ability to implement quick changes in their programming, one main question arises: how well equipped are the MDBs serving the region nowadays? To answer this question, we review the current situation of the main MDBs working in LAC.

At the World Bank, the last capital increase was obtained in 2018, before the crisis, enabling a significant credit expansion without compromising the financial profile. The World Bank's variation in commitments to the region between 2019 and 2020 has been the largest across MDBs serving LAC. This highlights the importance of being adequately capitalized to face regional needs during crises.

CAF's last capital increase was agreed to in 2015. CAF's capitalizations differed from that of other MDBs in what they were decided and implemented relatively rapidly and not in the context of an adverse shock. They had high paid-in to callable ratios. Shareholders were supportive during LAC's boom in the aftermath of the GFC. They heavily capitalized the bank at the upper part of the cycle to use this lending capacity during the trough. If this support continues during crises and shareholders keep contributing to capital, CAF will most probably consolidate itself among the two main multilateral financing sources to the region. The recent incorporation of Mexico as a full member goes into that direction, increasing CAF's geographical scope and diversification. On the contrary, if shareholder support for members weakens (including the breach of the PCT), this can pose serious challenges to the institution. MDBs with mainly borrowers' shareholding, such as CAF and CABEI, seem to require relatively high volumes of capital (low leverage). Encouraging further membership and having a long-term capitalization plan may help evolve in that direction.

Contrary to CAF capitalization, IDB's (2010) took much longer to negotiate. It was formally decided in the aftermath of the GFC when non-borrowing countries were still in crisis. The capitalization had a low paid-in to callable ratio given the non-borrowers' lack of appetite to provide fresh capital to an institution focused primarily on middle-income countries. Once IDB was capitalized, it continued to

[24] As mentioned in the previous section, the S&P's methodology is the most transparent and easy to replicate. It used to be the most restrictive as well. Subsequent revisions have relaxed some of the most extrema assumption and now Moody's and Fitch methodologies are as limiting as S&P's. In Moody's methodology, the determinants of an MDB capital adequacy assessment are the asset to equity ratio, the risk-weighted average credit quality of the portfolio, and the non-performing to total assets ratio. Fitch evaluates creditworthiness by combining two factors: capitalization and risk profile.

lend at levels like those during the crisis. The ensuing lending expansion combined with substantial transfers to Haiti, the low paid-in received, and the deterioration of regional macroeconomic conditions seriously stressed IDB's balance sheet by the mid-2010s. By that time, the IDB implemented a series of actions to revamp its capital base. Two milestones were particularly important: the consolidation of the private-sector activities into the IDB Invest (also decided after a long period of discussions), and the merge between the concessional and non-concessional windows, resulting in a capital increase for the ordinary capital. After that, lending resumed its expansion.

With no capital increase in this decade, the IDB has maximized its response by speeding up disbursements and project reformulation. Capital increase negotiations for an institution such as the IDB take time, particularly with an even voting power between borrowers and non-borrowers and the presence of a major shareholder with veto power on capitalization decisions, who has been reluctant in the recent past to either contribute with capital or be diluted. Nevertheless, the IDB has just launched a capitalization discussion. It is still early in the process, but some preliminary information suggests that the proposal would be around $78 billion in callable and $2 billion in paid-in capital.[25] To stand up to the new challenges and lend $20 billion yearly, the IDB would probably need a capital increase significantly more meaningful than the previous one.

Looking into the future, LAC's access to MDBs will likely be compromised by strategic considerations beyond the financial strength of those MDBs. At the World Bank, the largest global response has come from IDA (which serves very few LAC countries). Accordingly, most of the actions (including debt-relief initiatives) have been focused on and will likely continue to benefit the World's poorest countries. RMDBs in LAC will then have to meet the bulk of countries' demands. There is then a strong rationale to keep LAC RMDBs adequately capitalized.

Until now, the launch of the capitalization discussions had been ad-hoc and depended on external dynamics and occasional shareholder appetite. To conduct meaningful discussions, RMDBs would benefit from periodical assessments of their capital needs and an agreement on how and under which conditions they require a capital increase. This type of conversation may contribute to the coordination among shareholders, and between them and MDB's management. They may help build compromises and exert peer pressure on shareholders to participate in capital increases or face dilution. The systematization of these processes could bring enormous benefits to the multilateral system.

C. Strong Coordination

The GFC proved that a coordinated approach among major shareholders to confront a crisis could be decisive. At that time, G-20's proactive decisions (including the promise of future capitalizations) induced MDBs to significatively expand their lending. On the contrary, the COVID-19 crisis erupted in a context marked by the resurgence of nationalism and mistrust of the multilateral system. In this context, international cooperation has been limited, contrasting with developed countries' ambitious domestic policies. Coordination among MDBs has become more complex due to their larger number and the more fragmented ownership structure (Artecona, et al., 2019).

There is a consensus in the international development community that strong coordination between MDBs would reinforce each institution's actions and increase efficiency. MDB activities often overlap when operating in the same countries, with limited coordination, if not competition, and duplicate efforts (Prizzon, et al., 2017). Operating in a more coordinated manner and working as a system allows MDBs to achieve better results. This is particularly important when tackling global public goods and address collective action problems. For example, improving the collaboration between the

[25] https://www.bloomberg.com/news/articles/2020-12-10/latin-america-development-bank-gets-boost-from-key-u-s-senators.

MDBs for financing climate change programs will likely increase efficiency in this key area. Besides operational alignment, analytic coordination, for instance, through the elaboration of joint country strategies, could help MDBs to diagnose countries' development challenges better.

Coordination among MDBs helps to scale up the mobilization of private financing for development. MDBs mobilize investors through syndications and other pooled funding structures. Along with MDBs own resources, associated advice and risk mitigation help crowd in private financing. Moreover, when MDBs invest in a novel or high-risk environment, an important demonstration effect can lead to additional projects and new investors. Coordination among MDBs allows mobilization more systematically than on a project-by-project basis. For example, by establishing joint mechanisms for risk mitigations, like common guarantees and risk insurance. MDBs can also structure pooled vehicles or co-investment platforms to reduce individual investor costs for project preparation and execution (WB, 2016).

Coordination among MDBs has allowed them to optimize their balance sheets. This is the case of the exposure exchange agreements (EEA). Under the EEA, MDBs swap parts of their sovereign exposures. In that way, MDBs (specially RMDBs) reduce their concentration risk by diversifying their portfolios toward other regions.[26] A portfolio guarantee is another tool to freed up lending space on MDBs' balance sheets that require coordination between shareholders and MDBs. Under this arrangement, a developed country offers a guarantee to cover loans on an MDB. As MDBs leverage their capital, a guarantee of $1 allows for increments of $3 in loans. Sweden has implemented this type of mechanism with the Asian Development Bank and the IDB.

MDBs should also tackle debt distress associated with the COVID-19 pandemic in a coordinated fashion. So far, most of the debt relief initiatives (notably the G20's DSSI) have focused on the world's poorest countries, leaving aside most LAC countries. As countries confront increasing needs derived from the long-lasting pandemic, MICs will inevitably enter into debt-related problems. As previously noted, the MDBs' non-concessional windows' balance sheets would be severely affected by debt forgiveness.[27]

To conclude, we briefly review some collective MDBs actions to tackle debt problems that will probably arise due to the pandemic in MICs. These actions and recommendations are generally oriented toward expanding fiscal access and obtaining more financing from international markets at better rates. One option (Landers, 2020) is to advocate for an MDB green sovereign debt guarantee scheme to help countries maintain market access and set the stage for a green recovery. Under this initiative, MDBs could guarantee sovereign bond issuances to help countries manage rollover risk on existing external private-sector debt and maintain market access over the longer term. To ensure that these guarantees offer benefits to poor and vulnerable populations, they could be earmarked for green or SDG bond issuances.

Another option (Cárdenas, 2020) proposes that central banks, in coordination with the IMF and the MDBs, establish a special-purpose vehicle (SPV) that would bridge the vast amount of currently available global liquidity and emerging economies' growing financing needs. Specifically, the SPV would issue bonds to be purchased by central banks under their quantitative easing (QE) programs and then lend the proceeds to emerging economies. The MDBs can provide the initial equity needed. They would also manage the structuring, oversight, and servicing of the new loans. The SPV's portion of the

[26] In 2015, the IDB, the African Development Bank and the WB concluded an arrangement whereby the three exchanged loan exposure among themselves in such a way that the total amount of the exposure was equivalent, but it reduced the country concentration at the RMDBs. In December 2020 IDB executed an EEA with the Asian Development Bank.

[27] Fitch Ratings clearly stated: "Suspension of sovereign debt payments owed to MDBs would be negative for their ratings unless they were fully compensated by their shareholders. Such a delay would affect an MDB's credit profile through three key metrics: first, the impairment of sovereign loans would constitute a breach of the MDB's preferred creditor status, which gives repayment of loans to MDBs priority in a sovereign debt crisis. Secondly, the ratio of impaired loans to gross loans, a key measure of credit risk in MDB asset portfolios, would increase. Thirdly, the suspension of debt payments would also adversely affect the MDB's cash flows and liquidity." See (https://www.fitchratings.com/research/sovereigns/suspension-of-debt-payments-to-mdbs-risk-to-ratings-22-04-2020).

loans would not be booked on the MDBs' balance sheets and would not affect their credit ratings. The SPV loans should be used only to address the COVID-19 emergency (including the recovery).

A final option (Lee, 2020) is to create a financial structure (a "stretch fund") to add to the model for the specific purpose of absorbing additional risk and increasing impact. This would be an off-balance sheet pool investment vehicle, purpose-built to take on more risk, which could be accessed by multiple MDBs to back up their countercyclical interventions. A fund like this can provide the capital to leverage MDBs intervention during crises. It could co-finance SG and NSG projects, provide guarantees, encourage mobilization, and take some of the risks embedded in MDBs operations. Such institutions would not take the burden of the interventions during troughs off the MDBs hands. Still, it would help mitigate the risk embedded into expanding lending in the middle of a recession, having a greater risk tolerance than MDBs. For this institution to be self-sustained, it should be correctly capitalized and include MICs into its final beneficiaries. These, too, could be shareholders.

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