INTERNATIONAL MONETARY FUND

IMF POLICY PAPER

May 13, 2016

THE CONSOLIDATED MEDIUM–TERM INCOME AND EXPENDITURE FRAMEWORK

IMF staff regularly produces papers proposing new IMF policies, exploring options for reform, or reviewing existing IMF policies and operations. The following documents have been released and are included in this package:

- The **Staff Report** on the Consolidated Medium-Term Income and Expenditure Framework was prepared by IMF staff and completed on April 14, 2016 as a background paper to the FY 2017–FY 2019 Medium-Term Budget and supplement to the Review of the Fund's Income Position for FY 2016 and FY 2017-2018. The paper was prepared for the Executive Board's consideration on April 20 and April 22, 2016, respectively.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Electronic copies of IMF Policy Papers
are available to the public from
http://www.imf.org/external/pp/ppindex.aspx

International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

THE CONSOLIDATED MEDIUM-TERM INCOME AND EXPENDITURE FRAMEWORK

April 14, 2016

EXECUTIVE SUMMARY

The medium-term income projections have been updated from the April 2015 outlook and the February review of the adequacy of precautionary balances. The main changes to the outlook stem from a more gradual rise in the SDR interest rates and lower surcharge income following the lowering of the surcharges threshold.

The revised projections still show a positive forecast for net operational income (and surcharges) over the medium term, albeit lower than projected a year ago. Lending income (excluding surcharges) is marginally higher compared with earlier estimates. Surcharge income is estimated to be lower, reflecting the adjustment of the surcharges thresholds following the implementation of quota increases under the 14th General Review. Projected income from the Fixed-Income Subaccount of the Investment Account and interest-free resources are expected to increase more gradually over the medium-term as market indicators now point to a slower rise in interest rates from their current low levels. The expenditure path includes an increase in real terms of about ½ percent in the net administrative budget for FY 2017 to accommodate rising costs for physical and IT security. Moreover, reflecting further upward pressure over the medium term and uncertainty about the scope for offsetting savings, the traditional baseline assumption of a constant real spending envelope in the outer years is complemented by an alternative scenario with a further moderate spending increase of 1½ percent, phased in over FY 2018–19. In addition, a lower projected U.S. dollar/SDR exchange rate increases the expenses in SDR terms.

The steady state analysis which illustrates the Fund's income position in a future low-lending environment has been updated and now reflects the recently endorsed floor for precautionary balances of SDR 15 billion. Assuming an SDR interest rate of 2.5-3.0 percent, the steady state projection yields a positive income-expenditure position.

A slower pace of reserve accumulation is now expected. Assuming an unchanged margin for the rate of charge, precautionary balances are now projected to reach about SDR 18 billion by FY 2022 compared with SDR 19 billion projected a year ago and at the time of the review of precautionary balances. This reflects mainly the effect of lower interest rates over the medium term, coupled with the impact of the changes in surcharges thresholds following the 14th General Review of Quotas.

Approved By
Andrew Tweedie (FIN) and Daniel Citrin (OBP)

Prepared by the Finance Department and the Office of Budget and Planning

CONTENTS

INTRODUCTION

1. This paper updates the consolidated income and expenditure outlook from April 2015 and the recent review of the adequacy of precautionary balances.[1,2] The paper incorporates and extends the income and budget projections in the companion papers.[3]

2. The paper is organized as follows. The first part of the paper presents the updated outlook for the Fund's consolidated income and expenditure through FY 2022. It begins with a review of the outlook for the Fund's medium-term income from lending and non-lending income sources, highlighting key changes since the last update in April 2015.[4] The paper then describes the medium-term expenditure outlook. The discussion of consolidated income and expenditures concludes with an update of the long-run income-expenditure position which, as in the past, provides an illustration of the steady state income position when lending income has returned to low levels as envisaged at the time the Fund's New Income Model was developed. The second part of the paper provides an update on the projected pace of accumulation of precautionary balances over the medium term including changes since the February review of the adequacy of precautionary balances.[5]

CONSOLIDATED INCOME AND EXPENSES

A. Medium-Term Income

3. The medium-term income outlook remains positive despite a decline in projected income from surcharges and expectations for a more gradual rise in investment returns. Net operational income before surcharges is now expected to provide only a modest buffer over expenditures through FY 2021, while net income including surcharges remains positive through FY 2022.

[1] See *The Consolidated Medium-Term Income and Expenditure Framework* (04/10/15).

[2] In February 2016 the IMF's Executive Board discussed the adequacy of the Fund's precautionary balances. See *The Review of the Adequacy of the Fund's Precautionary Balances* (1/26/16).

[3] See *Review of the Fund's Income Position for FY 2016 and FY 2017-2018* (04/08/16) and *FY 2017-2019 Medium-Term Budget* (03/24/16).

[4] Lending income comprises i) operational lending income earned from the basic rate of charge, service charges, and commitment fees; and ii) income from surcharges which is not included in operational income.

[5] See *The Review of the Adequacy of the Fund's Precautionary Balances* (1/26/16). Precautionary balances comprise the general and special reserves (except for amounts in the special reserve attributed to profits from the 2009-2010 gold sales of SDR 4.4 billion), and the Special Contingent Account (SCA-1). An adequate level of precautionary balances is an essential element in the strategy to mitigate credit risk and thereby protect the value of reserve assets that members place with the Fund.

4. Operational lending income is projected to be marginally higher over the medium term than projected in April 2015. One additional Stand-By Arrangement (SBA) and one outright purchase (under the RFI) with total access amounting to SDR 1 billion, have been approved by the Executive Board since April 2015.[6] The revised projections also reflect some rephasing of purchases and lower than expected early repurchases. In aggregate, these changes have increased the projected credit path by an average of SDR 0.9 billion a year, or about 2 percent, over the period FY 2016-21, thus increasing projected annual average income from the margin and service charges by about SDR 10 million over the medium term.[7,8]

5. Non-lending income which is comprised of investment income, the implicit returns on the Fund's interest-free resources, and reimbursements to the General Resources Account (GRA) is expected to rise more gradually over the medium term than projected earlier.

- **Income from the Fixed-Income Subaccount is expected to be significantly lower over the medium term than projected in April 2015.**[9] The rise in yields as implied by forward markets is now more gradual; the forward curve of the SDR interest rate, which takes into account the impact of the inclusion of the Chinese renminbi (RMB) in the SDR basket implies a rate of only 1.2 percent in FY 2021, compared with 1.5 percent estimated in April 2015; more recently, an SDR interest rate of close to 2 percent in FY 2021 was implied by market forwards at the time of the reviews of the SDR basket and the adequacy of precautionary balances.[10] In addition the projections now embody more conservative assumptions on the gains to be made from a broadened investment mandate for this portfolio.[11] While this downward revision in projected investment income from the subaccount of SDR 400 million over the next five years compared

[6] Excludes arrangements treated as precautionary by the authorities upon approval of the program.

[7] See *Review of Access Limits and Surcharge Policies* (01/27/16).

[8] Commitment fee income is only recognized at the expiration or cancellation of an arrangement. The fees for the two-year FCL and Precautionary and Liquidity Line (PLL) arrangements are included in income at the end of the two-year period.

[9] The Fixed-Income Subaccount has investments equivalent to the Fund's general and special reserves except for (i) amounts attributed to gold sales profits in the special reserve and (ii) amounts of the general and special reserve attributed to net income for which no currency transfer have been made from the GRA to the IA in FY 2014 and FY 2015, totaling SDR 2.6 billion. These amounts were retained in the GRA as an interim measure providing the Fund with time to review the strategic asset allocation for the Fixed-Income Subaccount. The review was completed in August 2015 and staff now proposes to transfer currencies equivalent to net income for FY 2016 and the prior two years, from the GRA to this subaccount.

[10] On November 30, 2015, the Executive Board completed the quinquennial review of the method of valuation of the SDR, and determined that the RMB will be added to the SDR basket effective from October 1, 2016. The RMB will be represented in the SDR interest rate basket by the three-month benchmark yield for China Treasury bonds.

[11] The April 2015 projections assumed that the fixed-income subaccount would attain a premium of 100 basis points over the SDR rate, as originally expected when the Fund's New Income Model was developed, by FY 2021. In August 2015 the Executive Board modified the investment strategy of the fixed income subaccount that had been in place since 2006. The objective for the subaccount return is to exceed the SDR interest rate over time while minimizing the frequency and extent of negative returns. The updated projections assume that a premium of 50 basis points is attained by FY 2021.

with the April 2015 projection mainly reflects lower expected returns, a slower build up in reserves over the medium term, due mainly to the decline in projected surcharge income (see below), also contributes to lower investment income.

- **The Endowment Subaccount is expected to incur a loss in FY 2016 but the medium term outlook is broadly unchanged.** The current negative returns stem largely from volatility in the equity markets during the year including the large fall in equity prices in January 2016. However, the medium term outlook is relatively unchanged and remains positive. The three-year funding period of the passively-managed portion of the gold endowment began in March 2014; the projections continue to reflect the expectation that the endowment will be phased-in quarterly and thus be fully operational during FY 2018 with the illustrative assumption of 3 percent payouts commencing in that year.[12,13] During the funding period, investment income earned from the subaccount is assumed to be retained in the endowment in accordance with the Rules and Regulations of the Investment Account (IA) and is therefore not included in the Fund's operating income.

- **Projected income from interest-free resources has been lowered in line with expected interest rate developments.**[14] The implicit returns on interest-free resources follow the downward shift in the projected path for the SDR interest rates thereby lowering projected interest-free income through FY 2021 by some SDR 70 million compared with the estimates made in April 2015, or by more than SDR 90 million from the estimates at the time of precautionary balances review.

6. The more gradual increase in investment income described above combined with a rise in expenses in SDR terms has lowered projected net operational income over the medium term. In FY 2016, estimated expenses are expected to marginally exceed income (before surcharges) and result in a small operational loss for the period. Commitment fees from two precautionary arrangements approved in FY 2015 will contribute significantly to operational income in FY 2017. Thereafter a steady, albeit slower, increase in investment income is expected to broadly offset a decline in income from the margin as the stock of credit outstanding declines, to yield a small positive net operational income on average through FY 2021 (Figure 1).

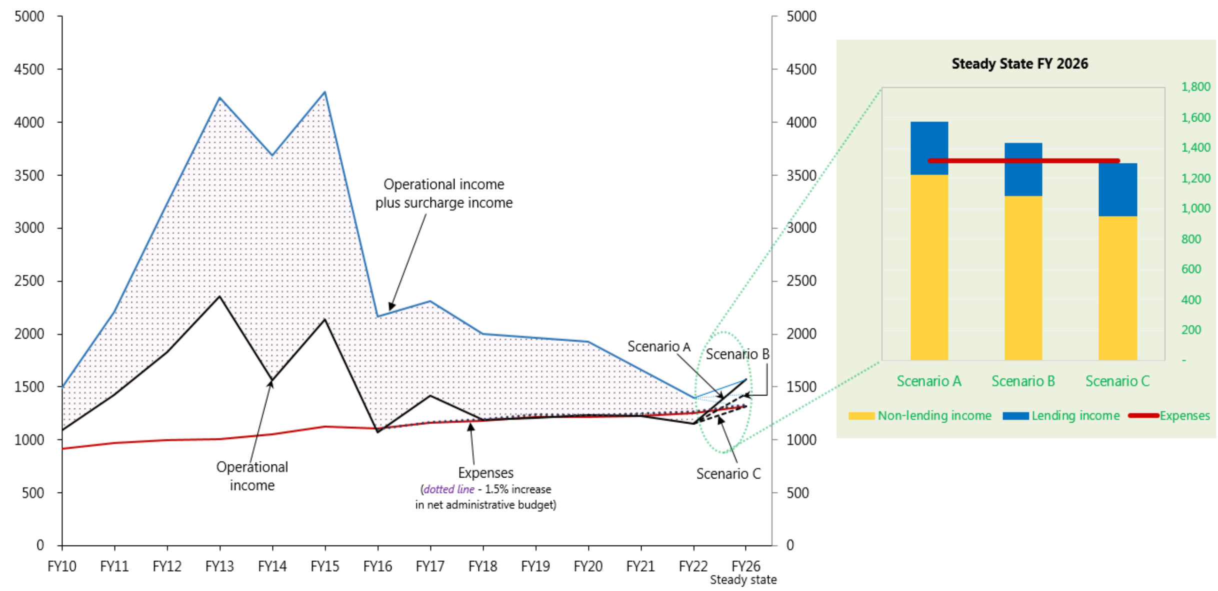
---

[12] It is expected that the Executive Board will consider the payout policy for the endowment toward the end of the phase-in period.

[13] The SDR rate is subject to a floor of 5 basis points (see *Recent fall in the SDR Interest Rate – Implications and Proposed Amendments to Rule T-1* (10/16/2014)), and as the low interest rate environment continues to prevail, actual returns on short-term deposits could fall short of the SDR rate in the near-term.

[14] GRA interest-free resources comprise primarily the SCA-1, unremunerated reserve tranche positions not represented by gold holdings, and GRA net income not transferred to the IA. These resources generate implicit income for the Fund by reducing members' reserve tranche positions and the remuneration expense thereon.

Figure 1. Actual and Projected Income and Expenses – FY 2010-2026 (in millions of U.S. dollars)



7. Surcharge income is projected to be significantly lower than the April 2015 estimates. Following the quota increases under the 14th General Review of Quotas, the Executive Board approved the adjustment of surcharge thresholds to 187.5 percent of quota and a shift of the time-based surcharge trigger for EFF arrangements to 51 months for all members with GRA credit outstanding.[15] As a result of these adjustments and the rephasing of purchases and the other assumptions noted above, annual surcharge income is projected to be lower by an average of about SDR 0.1 billion over the medium term compared with April 2015. Cumulative surcharge income over the period FY 2016-21 is now projected at SDR 3.3 billion.

8. The above projections include the expected impact of the inclusion of the Chinese renminbi (RMB) in the SDR basket. The Fund's lending income will not be affected by the increase in the SDR interest rate following the inclusion of the RMB in the SDR basket**.** The modestly higher rate of charge on Fund borrowings reflecting the increase in the SDR interest rate would be offset by the higher remuneration paid to Fund creditors on their reserve tranche positions or borrowed resources. However, the Fund's income position is expected to benefit marginally from a higher SDR interest rate as it translates into higher returns on the Fixed-Income Subaccount and to a lesser degree higher implicit returns on interest free resources. On this basis, a 17-20 basis point increase in the SDR interest rate would initially increase the Fund's income (through the investment account and implicit returns on interest free resources) by about SDR 35-40 million in FY 2018, the first full year following the inclusion of the RMB in the SDR basket.[16]

[15] See *Review of Access Limits and Surcharge Policies* (01/27/16).

[16] For a fuller discussion of the impact on the Fund's income of the inclusion of the RMB in SDR basket see *Review of the Fund's Income Position for FY 2016 and FY 2017-2018* (04/08/16).

9. The income projections outlined above remain highly uncertain and are sensitive to a number of key assumptions. Lending income is particularly susceptible to the timing of purchases and repurchases under existing arrangements, early repurchases, and possible new arrangements. Other key factors affecting the Fund's income position include fluctuations in global interest rates and the U.S. dollar/SDR exchange rate (Box 1 provides further details), and changes in actuarial assumptions that impact the annual pension expense under the amended International Accounting Standard 19 (IAS 19).[17]

B. Medium-Term Expenditures

10. The medium-term expense projections reflect a small increase in the net administrative budget in real terms, starting in FY 2017, to accommodate rising security costs. An additional $6 million is built into the FY 2017 administrative budget baseline to meet mounting costs for physical and IT security, which previously were met through reallocation and temporary financing. However, because the structural increase in the net administrative budget is mostly offset by a lower price deflator, the nominal expense path projections for the medium- and longer-term—assuming no further changes in spending volumes—are virtually unchanged from last year.[18]

11. The budget outlook, however, is subject to upward pressures. Additional resources will be required to implement the Global Policy Agenda, focused on strategically important initiatives in the areas of surveillance and capacity development. Also, in light of growing economic vulnerabilities in many member countries, the demand for Fund financing could continue to rise. Finally, future needs for physical and IT security and prospective revenue losses could also exert pressures on existing resources. As savings that can potentially be achieved through further reprioritization might not be sufficient to offset the higher spending, Figure 1 also shows an alternative scenario incorporating an additional permanent 1.5 percent increase in the net administrative budget, phased in over FY 2018-19. As illustrated, the impact of such an increase on the net income position would be marginal.

12. Capital expenditures remain elevated due to the HQ1 renovation. The expense path is slightly higher than assumed last year, as a result of the supplemental funding that was approved in January. However, the increase in capital expenses reflected in the Fund's income statement is

[17] IAS 19 (amended) is the International Financial Reporting Standard that deals with accounting for pension and other employee benefits, including the timing adjustment. The actuarially determined timing adjustment in FY 2016 results in a projected gain of about SDR 296 million, and stems mainly from a decline in the obligations of the staff retirement plan that reflect the outcome of a comprehensive review of actuarial assumptions. As discussed in the *Review of the Fund's Income Position for FY 2016 and FY 2017-2018* (04/08/16), the new standard was expected to introduce an additional source of volatility in the Fund's income over the medium-term; following the elimination of the corridor method, gains or losses arising from changes in actuarial assumptions are to be recognized in the year incurred.

[18] For FY 2017-19, the applied Global External Deflator is 1.9 percent, 2.2 percent, and 2.3 percent, respectively (For specific details, see *FY2017-2019 Medium-Term Budget* (March 24, 2016)). A five-year backward-looking average of the GED is used for the nominal long-term expense path.

projected to be moderate, as the major building renovations are depreciated over the remaining useful life of the building.

C. The Long-Run Income-Expenditure Position

13. The steady state outlook continues to point to a balanced position in a future low credit environment. In 2008, when the Board endorsed the New Income Model (NIM), a long-term goal was to broaden income sources to provide sustainable financing for the institution. In the current environment of very low interest rates, the Fund remains reliant on income from lending to cover the bulk of its activities. Against this background, the updated illustrative steady state outlook is intended as a cross-check on the consistency of the projected budgetary envelope with Fund income when lending income is assumed to be again at low levels. As such, the scenarios take into account the progress that has been made in implementing the NIM and the recent review of the adequacy of the Fund's precautionary balances. While all elements of the NIM are now in place or in progress, the global economic and market environment remains very different from that assumed when the NIM was agreed, indicating some risks if returns remained at low levels for a prolonged period.

14. The illustrative steady state is assumed to be reached in FY 2026 when drawings under current arrangements have been largely repurchased. The conservative assumptions underlying the steady state are intended to illustrate a possible floor level of income providing an indication of the Fund's ability to generate a net positive income position even when credit is low. Following the discussion of the adequacy of the Fund's precautionary balances in February 2016, a higher but still conservative credit level of SDR 20 billion is assumed in this illustrative low-lending environment (see Table 1).[19] Commitments under contingent lending facilities are also assumed to decline from current levels to SDR 10 billion (see Box 1). Assuming a margin of 100 basis points, lending income would, depending on the buoyancy of investment income, contribute in the range of 22 to 26 percent of total income.

15. Investment income would under most scenarios cover the bulk of expenses (Table 1). Investment income would be in the form of payouts from the Endowment Subaccount, currently assumed at 3 percent, and returns from the Fixed-Income Subaccount. The scenarios also assume precautionary balances at the new higher floor of SDR 15 billion that was broadly endorsed in the recent review, implying that the resources available to invest in the Fixed-Income Subaccount and thus investment income would both be higher at given rates of return.[20] On this basis, assuming a SDR interest rate of 3 percent and investment returns on the Fund's Fixed-Income Subaccount of an additional 50 basis points, the steady state projection yields a positive income-expenditure position with a relatively comfortable buffer of over SDR 180 million (over US$250 million) or about 20 percent of expenditures and, as also envisaged under the NIM, the Fund would not be relying on lending

[19] See *Review of the Adequacy of the Fund's Precautionary Balances* (1/26/16).

[20] Since the floor is below the projected level of precautionary balances over the medium term, the longer term steady state projection implicitly assumes a prior distribution of reserves that lowers precautionary balances to the level of the floor.

income to finance its non-lending activities (Scenario A). Assuming an SDR interest rate of 2.5 percent in keeping with the current low interest rate environment and the more gradual rise in interest rate projections, the steady state projection maintains a positive income-expenditure position but with a reduced margin of under SDR 90 million or about US$120 million (Scenario B). At an SDR interest rate of 2 percent, which would imply a near zero real interest rate (Scenario C) the steady state projection yields a slightly negative income-expenditure position. Under the alternative scenario, incorporating an additional permanent 1.5 percent increase in the net administrative budget, the impact on the steady state net income position is expected to be marginal (Figure 1 above).

Table 1. Consolidated Income and Expenses, FY2016–26
(in millions of U.S. dollars, unless otherwise stated)

	FY 16	FY 17	FY 18	FY 19	FY 20	FY 21	FY 22	FY 26	FY 26	FY 26
								Scenario		
								A (3%)	**B** (2.5%)	**C** (2%)
Based on updated thresholds following effectiveness of the 14th General Review of Quotas 1/										
I. Operational income	1,066	1,418	1,187	1,213	1,236	1,231	1,156	1,570	1,434	1,300
Lending income	893	1,260	700	638	554	441	308	347	347	347
Non-lending income	173	158	487	575	682	790	848	1,223	1,087	953
II. Expenses 2/	1,106	1,165	1,185	1,221	1,215	1,229	1,250	1,314	1,314	1,314
Of which: Net administrative budget 3/	1,040	1,072	1,096	1,127	1,138	1,155	1,178	1,245	1,245	1,245
III. Net operational income (I - II)	-40	253	2	-8	21	2	-94	256	120	-14
IV. Surcharges	1,095	895	814	752	690	430	242	0	0	0
V. Net income plus Surcharges (III + IV)	1,055	1,148	816	744	711	432	148	256	120	-14
Memorandum items:										
Fund credit (average stock, SDR billions)	51.5	49.4	47.4	44.9	39.6	31.5	22.0	20.0	20.0	20.0
US$/SDR exchange rate	1.39	1.40	1.40	1.40	1.40	1.40	1.40	1.40	1.40	1.40
Precautionary balances (end of period, SDR billions) 4/	15.2	16.1	16.7	17.2	17.7	18.0	18.1	15.0	15.0	15.0

1/ Following the Board discussion of the *Review of Access Limits and Surcharge Policies* (01/20/2016) paper on February 17, 2016, the trigger for time-based surcharges was moved to 51 months for EFF arrangements and the surcharges threshold for level-based surcharges was set at 187.5 percent of quota. Commitment fee thresholds are set at 115 percent, 116-575 percent, and greater than 575 percent of quota for charges of 15 basis points, 30 basis points, and 60 basis points, respectively.
2/ Includes: (i) net expenditures made from the administrative budget; (ii) expenditures made from the capital budget for items that are not depreciated; and (iii) depreciation charges for expenditures made from the current or previous capital budgets.
3/ FY 2016 net administrative budget is updated for the estimated outturn.
4/ Annual net operational income and surcharges add to the level of precautionary balances each year.

16. The steady state remains sensitive to other key assumptions, including the margin. While expenditures are assumed to be constant in real terms, the outlook remains sensitive to movements in the U.S. dollar/SDR exchange rate. The scenarios also assume that none of the credit outstanding in a low lending environment would be subject to surcharges. As such, a change in the margin could have a significant impact on the net income position particularly if interest rates were to remain low. Lowering the margin by 20 basis points to 80 basis points would reduce steady state income by SDR 40 million or US$56 million.

PRECAUTIONARY BALANCES OUTLOOK

17. The projected contribution of total lending income to the Fund's medium-term finances has been lowered from earlier estimates reflecting a steady decline in Fund credit outstanding. However, lending income including surcharges continues to contribute significantly to the accumulation of precautionary balances and net income (excluding projected losses of the gold endowment) is projected at about SDR 1.1 billion in FY 2016 (see Table 2). When placed to reserves, this would increase precautionary balances to reach about SDR 15.2 billion by end-FY 2016.

18. The slower projected pace of reserve accumulation over the medium term largely reflects reduced income from surcharges and a more gradual rise in investment income. The April 2015 baseline projections, which assumed a margin on the rate of charge of 100 basis points (the current level), and no change in quotas or surcharge thresholds had indicated that precautionary balances would reach about SDR 19 billion in FY 2022, slightly below the SDR 20 billion indicative target (Figure 2, Panel A). An updated medium-term path for precautionary balances was discussed in February 2016 in the context of the review of the adequacy of precautionary balances.[21] Although projections at the time of that review factored in a reduction of surcharge income on the assumption that thresholds were not set to fully offset the impact of the quota increase, (Figure 2, Panel A), the projected accumulation of precautionary balances remained broadly in line with the April 2015 projections. Expected losses from lower surcharge income were largely offset by slightly higher investment income reflecting a more rapid rise in the SDR rate implied by market futures at the time.

19. The April 2016 income projections have been further lowered compared with prior projections. This reflects a downward adjustment in the SDR interest rate path since the February precautionary balances review lowering investment income returns over the medium term, and the higher expenses in SDR terms following the medium-term U.S. dollar/SDR exchange rate projection being revised from US$1.48 per SDR to US$1.40 per SDR. Against this backdrop, the pace of reserve accumulation has slowed down further.[22] At the reduced pace of reserve accumulation currently projected, precautionary balances are expected to reach SDR 18.1 billion in FY 2022 (Figure 2, Panel A), remaining below the indicative medium-term target of SDR 20 billion. Under a scenario where the margin is increased to 120 basis points precautionary balances would rise to about SDR 18.6 billion, but still remain at least SDR 1 billion below the target over the medium term (see Figure 2, Panel B). Conversely, if the margin were reduced to 80 basis points, projected accumulation of precautionary balances would be lowered by about SDR 500 million to SDR 17.6 billion. The IAS 19

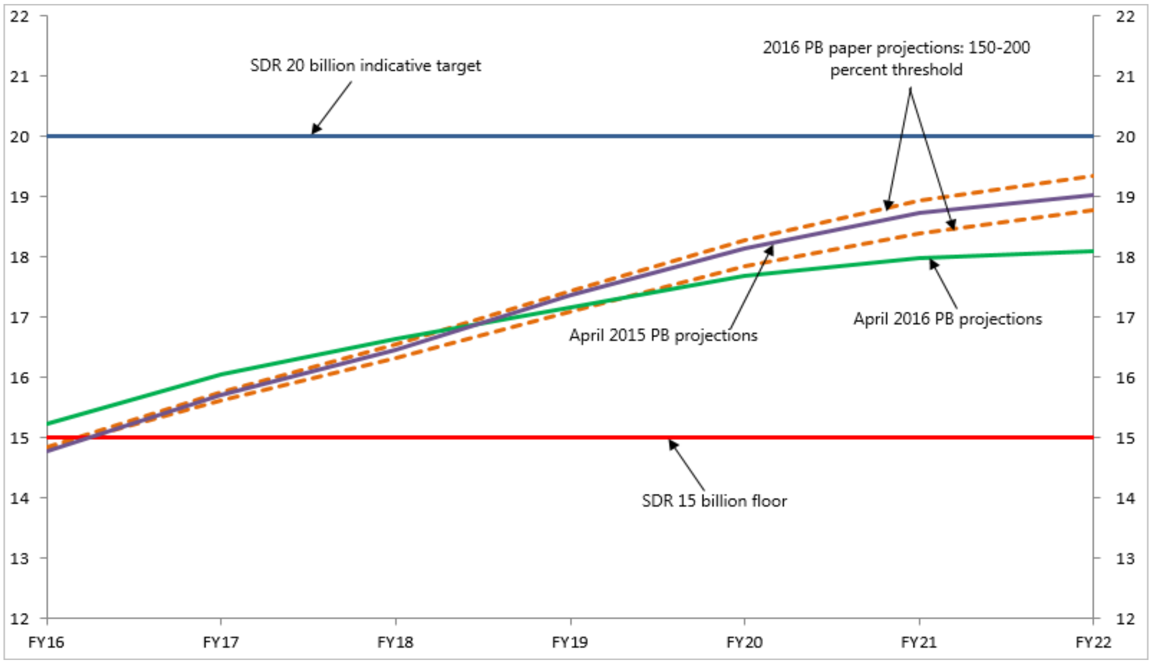
[21] At the review the Board agreed to maintain the indicative medium-term target of SDR 20 billion. See *Review of the Adequacy of the Fund's Precautionary Balances* (1/26/16) and *The Acting Chair's Summing Up Review of the Adequacy of the Fund's Precautionary Balances Executive Board Meeting 16/15 February 19, 2016* (02/25/16).

[22] The pace of reserve accumulation has been impacted by the changes in the Fund's structure and thresholds of surcharges and commitment fees following the effectiveness of the 14th General Review of Quotas. See *Review of Access Limits and Surcharge Policies* (01/27/16).

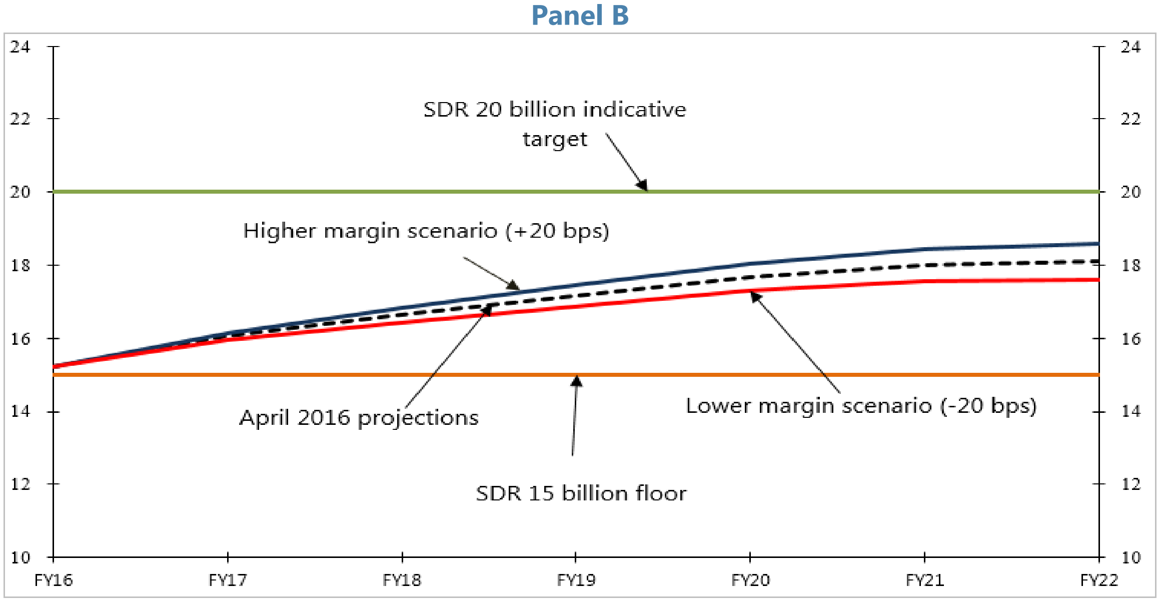
timing adjustment is also expected to remain volatile and affect the pace of reserve accumulation over the medium term.[23]

Figure 2. Precautionary Balances Accumulation
(in billions of SDRs)

Panel A



Panel B



[23] Since the IAS 19 timing adjustment is sensitive to changes in the discount rate and the fair value of pension assets, the effects of which are highly unpredictable over the medium term, no projections are made beyond the current financial year-end (FY 2016).

Table 2. Consolidated Income and Expenses, FY2016–26
Updated thresholds following 14th General Review of Quotas [1]

	FY16	FY17	FY18	FY19	FY20	FY21	FY22	Scenario A SDRi 3% FY26	Scenario B SDRi 2.5% FY26	Scenario C SDRi 2% FY26
	(in SDR millions)									
A. Operational income 2/	**767**	**1,014**	**848**	**866**	**884**	**879**	**826**	**1,121**	**1,025**	**929**
Lending income	643	901	500	456	396	315	220	248	248	248
Margin for the rate of charge	515	494	474	449	396	315	220	200	200	200
Service charge	32	19	9	7	0	0	0	24	24	24
Commitment fees	96	388	17	0	0	0	0	24	24	24
Investment income	59	41	260	310	376	441	473	651	582	513
Fixed-Income Subaccount 3/	59	41	117	165	228	290	319	484	415	346
Gold endowment pay-out	0	0	143	145	148	151	154	167	167	167
Interest free resources 4/	8	17	33	43	54	64	73	157	130	103
SCA-1 and other	8	17	33	43	54	64	73	157	130	103
Reimbursements	57	55	55	57	58	59	60	65	65	65
CCR Trust and SDR Department	7	5	4	4	4	4	4	6	6	6
PRG Trust	50	50	51	53	54	55	56	59	59	59
B. Expenses	**795**	**833**	**846**	**872**	**869**	**877**	**893**	**938**	**938**	**938**
Net administrative budget 5/	748	766	783	805	813	825	841	889	889	889
Capital budget items expensed	20	30	23	25	12	7	7	6	6	6
Depreciation	27	37	40	42	44	45	45	43	43	43
C. Net operational income (A-B)	**-28**	**181**	**2**	**-6**	**15**	**2**	**-67**	**183**	**87**	**-9**
Surcharges	788	639	581	537	493	307	173	0	0	0
IAS 19 timing adjustment	296	0	0	0	0	0	0	0	0	0
Endowment (Gold Profits) Subaccount 6/	-58	198	95	97	99	101	103	112	112	112
Net income	**998**	**1,018**	**678**	**628**	**607**	**410**	**209**	**295**	**199**	**104**
	(in US$ millions)									
D. Operational income 2/	**1,066**	**1,418**	**1,187**	**1,213**	**1,236**	**1,231**	**1,156**	**1,570**	**1,434**	**1,300**
Lending income	893	1,260	700	638	554	441	308	347	347	347
Investment income	82	57	363	435	527	619	663	912	815	718
Interest free resources	12	23	46	61	75	89	102	220	181	144
Reimbursements	79	78	78	79	80	82	83	91	91	91
E. Expenses	**1,106**	**1,165**	**1,185**	**1,221**	**1,215**	**1,229**	**1,250**	**1,314**	**1,314**	**1,314**
Net administrative budget	1,040	1,072	1,096	1,127	1,138	1,155	1,178	1,245	1,245	1,245
Capital budget items expensed	28	41	33	35	16	10	9	9	9	9
Depreciation	38	52	56	59	61	64	63	60	60	60
F. Net operational income (D-E)	**-40**	**253**	**2**	**-8**	**21**	**2**	**-94**	**256**	**120**	**-14**
Memorandum Items:										
Fund credit (average stock, SDR billions)	51.5	49.4	47.4	44.9	39.6	31.5	22.0	20.0	20.0	20.0
SDR interest rate (in percent)	0.1	0.3	0.6	0.8	1.0	1.2	1.4	3.0	2.5	2.0
US$/SDR exchange rate	1.39	1.40	1.40	1.40	1.40	1.40	1.40	1.40	1.40	1.40
Surcharges (US$ millions)	1,095	895	814	752	690	430	242	0	0	0
New income measures (US$ millions) 7/	73	82	307	334	362	391	405	478	478	478
Precautionary balances (end of period, SDR billions)	15.2	16.1	16.7	17.2	17.7	18.0	18.1	15.0	15.0	15.0

[1] Following the Board discussion of the *Review of Access Limits and Surcharge* Policies (01/20/2016) paper in February 2016, the trigger for time-based surcharges was moved to 51 months for EFF arrangements and the surcharges threshold for level-based surcharges was set at 187.5 percent of quota. Commitment fee thresholds are set at 115 percent, 116-575 percent, and greater than 575 percent of quota for charges of 15 basis points, 30 basis points, and 60 basis points, respectively.
[2] Excludes surcharges. The payout from the endowment funded by gold profits is assumed to begin in FY 2018, when the endowment is fully funded under the agreed investment mandate.
[3] The current projections assume that a premium of 50 basis points over the SDR rate is attained by FY 2021 and that the premium remains at this level thereafter.
[4] Interest free resources reduce the Fund's costs and therefore provide implicit returns. Since the Fund invests its reserves in the IA to earn a higher return, the interest free resources retained in the GRA are mainly attributable to the SCA-1, unremunerated reserve tranche positions not represented by gold holdings, and GRA income for the year not transferred to the IA. These resources reduce members' reserve tranche positions and the Fund's remuneration expense resulting in implicit income for the Fund.
[5] For FY 2016, the figure represents estimated net administrative expenditures, which are slightly lower than the budget.
[6] From FY 2018 when the endowment is fully in place, it is assumed that the endowment is to make an annual payout to the GRA and that a portion of the income is to be retained to preserve the real value of the gold endowment.
[7] The effect on operational income of broadening investments, creating an endowment funded by profits from gold sales, the reduction in remuneration from proceeds equal to the book value of gold, and reimbursement of PRGT expenses.

Box 1. Income Projections

Key Parameters	Key Parameters	Key Parameters
US$/SDR exchange rate	1.40	Assumed unchanged from recent levels. A 10 percent rise (fall) in the US$/SDR exchange rate would raise (lower) annual income in FY 2022 by US$120 million.
SDR interest rate	Rising to 3.0 percent by FY 2026 from 0.1 percent in FY 16	A 10 basis point higher (lower) average SDR interest rate would raise (reduce) annual income in FY 2022 by US$34 million. In the steady state a 10 basis point higher/lower SDR interest rate would raise/reduce income by SDR 27 million.
Margin for rate of charge (basis points)	100	Assumed unchanged from current level. A 20 basis point higher (lower) margin would increase (reduce) income in FY 2017 and FY 2018 by US$138 million and US$134 million, respectively. A 20 basis point higher (lower) margin effective from FY 2017 would increase (lower) precautionary balances in the period to end-FY 2022 by some SDR 0.5 billion.

Operational lending income (US$347 million or SDR 248 million by FY 2026)

Fund credit is assumed to decline to an average steady state level of about SDR 20 billion by FY 2026, upon which a margin of 100 basis points would generate income of about SDR 200 million. Commitments under contingent lending facilities are assumed to also decline to an average of SDR 10 billion in the steady state, yielding some SDR 24 million in annual commitment fees. Average annual disbursements of about SDR 5 billion from FY 2023 generate about SDR 24 million in annual service charges (at 50 basis points).

Investment income (US$912 million or SDR 651 million by FY 2026)

Currency amounts equivalent to net operational income plus surcharges are assumed to be transferred annually to the Fixed-Income Subaccount for investment in the subsequent year. Phased investments under the broadened investment mandate for the Fixed-Income Subaccount is assumed to be begin in FY 2017, allowing average investment returns in this portfolio to exceed the SDR interest rate by 50 basis points from FY 2021 onwards. This would yield annual income of about SDR 484 million in the steady state (FY 2026) assuming an SDR interest rate of 3 percent (Scenario A) and precautionary balances floor of SDR 15 billion endorsed in the recent review of the adequacy of precautionary balances.

The updated projections assume that implementation of the proposed investment strategy for the endowment (SDR 4.4 billion, equivalent to an average gold price of US$850 per ounce, plus earnings during the interim period) will continue to be phased-in gradually with assumed annual payouts of 3 percent beginning in FY 2018.[1/]

Interest free resources (US$220 million or SDR 157 million by FY 2026)

The interest free resources retained in the GRA are mainly attributable to the SCA-1, unremunerated reserve tranche positions not represented by gold holdings, and GRA net income not transferred to the Investment Account. These resources reduce members' reserve tranche positions and the Fund's remuneration expense resulting in implicit income for the Fund.

Reimbursements (US$79 million or SDR 57 million in FY 2016)

Reimbursements from the SDR Department and CCR (formerly PCDR) Trust, are projected at about SDR 7 million in FY 2016 and reimbursement of the GRA for the expenses of administering the PRGT is assumed to be SDR 50 million in FY 2016. Administrative costs and the associated reimbursements are assumed to be stable in real terms in the medium term.

1/ Staff plans to return to the issue of an appropriate payout policy before the end of the phase-in period of the passively-managed portfolio.