Introduction

The coronavirus pandemic continues to unfold as an unprecedented global crisis. The pandemic has created devastating rates of infection, mortality and lasting health impacts, exacerbated the fragility in health systems, and disrupted the provision of primary healthcare. Beyond these health impacts, the global pandemic has severe socio-economic consequences, including the broadest collapse in per capita incomes since 1870, the loss of 495 million jobs in Q2 2020, protracted school shutdowns, and now the risk of famine and violent conflict. The direct and secondary effects of the pandemic are disproportionately affecting the poorest and most vulnerable populations, with the level and depth of poverty rising for the first time in three decades. It is likely that the worst effects of the pandemic are yet to be seen.1

The United Nations Office for the Coordination of Humanitarian Affairs (OCHA) estimates the need for an additional $90 billion in financing for low-income countries2—a less than 1 per cent of the stimulus packages currently being implemented in OECD countries. It is cheaper, more effective and more dignified for people in crisis to act now. Further delays in the global response will increase the cost of the crisis. In an interconnected and globalized world economy, the effects of the crisis, if left unaddressed, are likely to cascade and reverberate for years to come.3

The current existing funds and commitments from International Financial Institutions (IFIs)4 fall short of what is needed to overcome this crisis. While OECD countries are rewriting the rulebooks when it comes to their own public finances, the financial instruments available to the most vulnerable countries are more limited. Based on publicly available information compiled by the Centre for Disaster Protection and OCHA5, IFIs have committed $87 billion in COVID-19 response financing worldwide, as of 8 October.6 This still falls short of the needs of the pandemic response, with the financing also not well targeted at those countries most in need.

1 The pandemic presents one of the broadest humanitarian crises in decades, as reflected in the following projected scenarios. If no action is taken, the World Bank estimates the COVID-19 pandemic alone is estimated to push an additional 100 million (range: 88 million to 115 million people) into extreme poverty this year, with the total rising to as many as 150 million by 2021, depending on the severity of the economic contraction. At the US$3.20-a-day poverty line, between 175 million and 223 million people are estimated to be pushed into poverty. The number of people who are acutely food insecure is projected to increase by 82 per cent—or 121 million people—to 270 million people by the end of 2020, according to WFP. For poverty projections, see World Bank, "Poverty and Shared Prosperity 2020: Reversals of Fortune," Washington DC: World Bank Group (October 2020). For food insecurity projections, see World Food Programme, "WFP Global Response to COVID-19: June 2020" (June 2020).
2 This estimate refers to financing need for low-income countries, as defined by the World Bank 2019-2020 classifications. The countries include: Afghanistan, Benin, Burkina Faso, Burundi, Central African Republic, Chad, Congo DR, Eritrea, Ethiopia, Gambia, Guinea, Guinea-Bissau, Haiti, Korea DPR, Liberia, Madagascar, Malawi, Mali, Mozambique, Nepal, Niger, Rwanda, Sierra Leone, Somalia, South Sudan, Syrian Arab Republic, Tajikistan, Tanzania, Togo, Uganda, Yemen, and Zimbabwe.
4 International Financial Institutions (IFIs) are multilateral, regional and national development banks with international operations, including the IMF, World Bank, Asian Development Bank (ADB), African Development Bank (AfDB), Inter-American Development Bank (IDB) and Islamic Development Bank (IsDB) and regional development banks.
5 The data is currently hosted on three platforms:
6 Excluding two large-scale flexible credit lines to Peru and Colombia. Note that these figures include COVID-19-specific grant and lending that has been committed by the IMF, World Bank, Asia Development Bank (ADB), African Development Bank (AfDB), European Commission (EC), Inter-American Development Bank (IDB), and Islamic Development Bank (IsDB).
that need it most. Approximately 12 per cent ($10.6 billion) of all COVID-19 financing has been committed to low-income countries. Nearly all financing has taken the form of loans rather than grants (95 per cent). After peaking in June, new monthly financial commitments for COVID-19 have fallen, with a total of $1.87 billion committed in September – only 6.6 per cent of that in June ($28 billion).

**IFIs need to act ambitiously and act now – and to boldly use creative solutions to expand the use and capability of existing resources.** There is a strong moral and economic case for the international community to coordinate an immediate scale-up of financial resources to respond to the COVID-19 crisis. Against this backdrop, this report calls for shareholder support for four policy options that IFIs and multilateral development banks (MDBs) can use to meet the financing needs of the COVID-19 response:

1. **Use existing commitments and limits fully.** MDBs should deliver on all commitments to increase the speed of disbursements and the transparency of reporting. MDBs should recognize the value of callable capital commitments to increase their lending capacity to an estimated $1 trillion. Countries should deliver on their ODA commitments. These additional resources could be used to replenish the IDA window ahead of schedule and would provide an important signal to the market of future financing needs.

2. **Expand Special Drawing Rights.** A new general allocation of SDRs equivalent to $500 billion would result in an allocation of $22 billion to low-income countries – equivalent to a 9 per cent increase in international reserves. There is also scope to reallocate unused SDRs concurrently to funds that support low-income countries, such as the Poverty Reduction and Growth Trust. However, member states must achieve the necessary political support to enable this option.

3. **Rethink outstanding debt and new debt relief packages.** There should be a coordinated effort between private and official creditors to (1) implement a universal debt standstill and (2) to initiate concrete and systematic efforts towards debt restructuring for longer term debt sustainability. International financial regulatory bodies should play a coordinating role to ensure creditors and debtors have the breathing space to take meaningful steps to rethink debt and mitigate fear of downgrades due to participation in the DSSI. The DSSI should be extended to at least the end of 2021 and steps should be taken now to put in place a mechanism for debt relief in the future.

4. **Leverage differential pricing to improve the terms of lending.** Differential pricing should be leveraged to improve the terms of lending for low- and lower-middle income countries. While this option may not generate the same magnitude of funding as the aforementioned options, it is an important step towards building a sustainable international financial system.

**These options are technically feasible and non-mutually exclusive.** They can and should be implemented in tandem, to expand the support for low and lower middle-income countries in their response to the COVID-19 pandemic. Clear and unified support from IFI shareholders will be key to delivering on the promise of these options. An increase in liquidity, especially in the form of direct budget support, would help vulnerable countries navigate through the crisis. **IFIs should use real-time data to ensure this financing reaches the most vulnerable populations.** We recognise the challenge in this, but it is clear that an injection of liquidity now will undoubtedly reduce humanitarian need later.

**Option 1. Using existing commitments and limits fully**

**Key takeaway:** MDBs should deliver on all commitments to increase the speed of disbursements, and the transparency of reporting. MDBs should recognize the value of callable capital commitments to increase their lending capacity to an estimated $1 trillion. Countries should deliver on their ODA commitments and these additional resources could be used to replenish the IDA window ahead of schedule and would provide an important signal to the market of future financing needs.
Multilateral Development Banks (MDBs) should increase the pace of disbursements for funds already committed to the pandemic. Anecdotal evidence suggests disbursements remain far below commitments across the board. Based on publicly available data, only 69 per cent of committed financing for the COVID-19 response had been disbursed by 8 October 2020. For funding to be impactful it is important that commitments are converted into timely disbursement.

However, efforts to track these flows and hold MDBs accountable have suffered because of a lack of transparent reporting. The World Bank has made significant progress in transparency through their monthly releases of disbursement data, which enable us to track their rate of disbursement. However, publicly available data on disbursements is significantly lacking for other MDBs, so it is difficult to conduct a full assessment of progress. For example, MDBs were excluded from the G20 Debt Service Suspension Initiative (see Option 3 below), conditional on a promise that they would disburse more in every country than they were going to receive in debt service repayments over the DSSI period. However a lack of data on disbursements has made it difficult to assess whether or not MDBs have been following through on this promise.

MDBs should release regular updates on their disbursements (and not only their commitments) by country and by month or quarter. To hold MDBs accountable, an independent and trusted institution should be assigned to track and report these disbursements. MDBs would need to agree to send their data to the mediating institution. The mediator would in turn ensure data consistency. Greater speed and transparency in disbursements by MDBs would generate more leverage to advocate for the other financing options listed in this report that require shareholder support, such as replenishing the IDA.

In addition to delivering on existing commitments, MDBs can scale up their resources by an additional $531 billion above current exposures, within their current statutory limits. To reach this estimated ‘surge’ capacity, shareholders would have to recognize the value of callable capital commitments as a part of the MDB shareholder backstop. Doing so would increase the aggregate exposures of MDBs by almost two-fold, bringing lending capacity to around $1.1 trillion. In a similar vein, the S&P have previously estimated that MDBs could afford to increase their lending exposure by 72 per cent within their current credit ratings in aggregate. For instance, while maintaining top credit ratings and stable outlooks, the leverage ratio of MDBs could be incrementally increased by 0.1 every five years from 1 to 1.5. During the global financial crisis, these institutions demonstrated some willingness to do this with the support of their country shareholders. There is scope and need for shareholder support to do more now.

Moreover, donors should deliver on Official Development Assistance (ODA) commitments made in the past. In 2019, only five countries out of the 30 members of the Development Assistance Committee reached the target of spending 0.7 per cent of gross national income on aid. While total ODA increased last year, as a

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7 These estimates were derived from a publicly available dataset compiled by the Centre for Disaster Protection and UN OCHA, available here and here.

8 This agreement was made in light of the fact that MDBs rely on inflows of debt payments to replenish and fund future financial outflows.


10 This proposal rests on the assumptions that institutions remain within their current triple-A credit rating. Going beyond the current proposition, IFIs could even risk a downgrade to AA in order to provide more funding, although this proposal is likely to be met with heavy resistance from shareholders.

A general allocation of $500 billion of SDRs would increase total international reserves by 4.5 per cent. The level of ODA for this year is likely to decrease further with falling GDPs in donor countries. Therefore, it is more important than ever for donors to deliver on the levels of ODA committed in the past. This would deliver approximately $200 billion of additional resources that could be used to target the current crisis.

**Option 2. Expand Special Drawing Rights**

**Key takeaway:** A new allocation of SDRs equivalent to about $500 billion would result in an allocation of $22 billion to low-income countries – equivalent to a 9 per cent increase in international reserves. There is also scope to reallocate unused SDRs concurrently to funds that support low-income countries, such as the Poverty Reduction and Growth Trust. However, member states must achieve the necessary political support to enable this option.

A new allocation of special drawing rights (SDR), an IMF reserve asset, can be used to increase the reserves of its members. In a general allocation of SDRs, members are allocated SDRs in proportion to their IMF quotas. While the SDR is not a currency, its value is determined by the market exchange rates of a basket of international currencies (the US Dollar, Euro, Chinese Renminbi, Japanese Yen, and Pound Sterling). Members can freely buy or sell SDRs to other members and claim SDRs for freely usable currencies for liquidity.

The scope of the current crisis calls for a large general allocation of SDRs equivalent to at least $500 billion. A general allocation of $500 billion of SDRs would increase total international reserves by 4.5 per cent.

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compared to the end of 2019, with an estimated $22 billion being directly allocated to low-income countries (equivalent to a 9 per cent increase in international reserves). More importantly, a general allocation would allow members with additional excess SDRs to transfer their holdings to vulnerable countries in exchange for credit, or alternatively, to transfer SDRs as resources to other IMF funds, such as the Poverty Reduction and Growth Trust (PRGT). Countries could make commitments to redistribute excess SDRs (to vulnerable countries or IMF funds) prior to a new general allocation in a way that ensures the final distribution of SDRs reaches countries that need it most.

A large-scale issue of SDRs is not an unprecedented policy. At the 2009 G20 summit in London, the IMF issued $250 billion of SDRs, a move that was central to mitigating the effects of the financial crisis. While some argued then, and now, that an SDR allocation would be inflationary, experiences during the global financial crisis show that inflation is unlikely to be a major concern during a global recession. The economic damage of COVID-19 has already surpassed that from the global financial crisis, and its consequences are likely to be even more long-lasting. Therefore, the general consensus remains that inflation should not be a concern when considering financing options.

Nor should the concern about conditionality delay a general SDR allocation. There exists a concern that liquidity support would be provided to every country, irrespective of their current political, human rights and environmental situation. This concern could be best addressed through the aforementioned commitment to distribute excess SDRs according to pre-defined and transparent criteria.

The proposal to issue a large general allocation of SDRs has been supported by the IMF Managing Director, Kristalina Georgieva, the G24, and has been advocated extensively by leading experts and academics. Nonetheless, IMF calls to create a new issue of $500 billion SDRs were vetoed by India and the United States at the G20 and IMF Spring Meetings. In recognition of the significant benefits of a general allocation, there should be a renewed effort to reach agreement on the proposal and achieve universal shareholder buy-in.

Beyond a large allocation, there is scope for member states to reallocate existing excess SDRs towards funds or facilities that support low-income countries in need, such as the PRGT. A similar policy was conducted in March 2016, during which around 95 per cent of the SDR distribution was pledged to the PRGT to subsidize lending to low-income countries. However, a general allocation would have a much more substantial and long-lasting impact. Member states must achieve the political support required for this option.

Option 3. Debt Relief and Restructuring – rethinking outstanding debt and new debt relief packages

Key takeaway: There should be a coordinated effort between private and official creditors to (1) implement a universal debt standstill and (2) to initiate concrete and systematic efforts towards debt restructuring for longer term debt sustainability. International financial regulatory bodies should play a coordinating role, to ensure that creditors and debtors have the breathing space to take meaningful steps to rethink debt and

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18 Yi Gang, “The IMF should turn to special drawing rights in its Covid-19 response”, Financial Times Opinion (16 July 2020), [https://www.ft.com/content/e7ef20-3960-46e7-922b-112da8f2def](https://www.ft.com/content/e7ef20-3960-46e7-922b-112da8f2def).


mitigate the fear of downgrades due to participation in the DSSI. The DSSI should be extended to at least the end of 2021 and steps should be taken now to put in place a mechanism for debt relief in the future.

Gross government debt in low-income countries has been rising since 2013. Concerns of debt sustainability prevalent prior to the pandemic have been exacerbated by current circumstances. As of 30 June 2020, 8 low-income countries were in debt distress, and a further 28 at high-risk of debt distress. On 23 September, Zambia announced it was seeking “the suspension of debt service payments for a period of six months” from private creditors holding around $3 billion in international bonds, possibly making Zambia the first African country to default on its debt due to the coronavirus pandemic. The looming threat of a broader debt crisis calls for a rethinking of outstanding debt and new debt relief packages.

In a first effort to reduce the debt burden, the G20 Debt Service Suspension Initiative (DSSI) allows eligible countries to suspend debt service repayments to bilateral official creditors from 1 May 2020 until the end of the year. This has the potential to release up to $11.5 billion in repayments that can be retargeted towards social, health, and economic spending for the pandemic. In October 2020, G20 bilateral official creditors agreed to extend the DSSI by six months until end of June 2021. The IMF, together with the World Bank, have expressed support for extending DSSI for even longer. The G20 have agreed to examine the need for a further extension by the time of the IMF–World Bank Spring Meetings in April 2021.

While this is a good first step, we argue below that there should be a coordinated effort between private and official creditors to (1) implement a universal debt standstill and (2) to initiate concrete and systematic efforts towards debt restructuring for longer term debt sustainability. This effort needs to be led and coordinated by international financial regulatory bodies, to ensure creditors and debtors have the breathing space to take meaningful steps to rethinking debt. There is an opportunity now to initiate these efforts as the conversation turns to the extension of the DSSI to the end of 2021.

While current debt relief initiatives have centred around official creditors, any further policies require meaningful cooperation and involvement from private creditors, including Western as well as Chinese banks, to deliver larger-scale debt relief. Among countries eligible for the DSSI, an estimated $13 billion of debt repayments between 1 May to 31 December 2020 are due to private creditors, compared with $11 billion from official bilateral lenders, and $7 billion from multilateral lenders. Without greater political coordination, there is fear that any debt relief from the DSSI would simply feed into servicing private debt, rather than injecting liquidity into funding programmes that address the mounting humanitarian crisis. This not only disincentivizes further debt relief from official creditors, but also undermines the overall impact of the initiative.

Furthermore, the lack of collective action has hindered the adoption of existing debt relief initiatives. Of the 73 countries eligible for support under the DSSI, only 60 per cent have made a request as of mid-October, generating the deferral of an estimated $5.0 billion of 2020 debt service—leaving up to £3 billion of untapped potential DSSI savings. While lack of participation could be for a variety of reasons, many countries have been hesitant to sign on due to the threat of credit downgrades and legal defaults that would further limit access to the international capital market. For instance, Moody’s has placed several countries on review for a downgrade, following participation in the DSSI. These responses are a direct result of the structural

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24 Estimates according to the Institute of International Finance. See White & Case LLP, “The G20 Debt Service Suspension Initiative—Reaction from key market participants,” Publications and Events (8 June 2020), https://www.whitecase.com/publications/alert/g20-debt-service-suspension-initiative-reaction-key-market-participants
25 Moody’s has put countries under review for a downgrade, as they argue that participation in the DSSI with official creditors increases the risk of countries requesting comparable terms to the DSSI with private creditors. While ratings agencies have stated that while they do not classify participation in debt relief with official creditors as a default, a similar agreement with a private creditor would be classified as default.
shortcomings of the international financial system. Credit ratings agencies are required to downgrade countries in the face of non-payment by their regulatory agencies; and furthermore, private banks are required to provision more heavily against downgrade risk.

Therefore, international financial bodies will need to initiate and coordinate a fair and equitable mechanism for regulatory forbearance. These regulatory conditions will be needed for a collective debt standstill from both private and official creditors. International regulatory bodies should take the lead in coordinating messaging that participation in the DSSI itself should not be qualify as a default and affect future credit ratings, thereby removing the stigma attached with participation.

These efforts need to be met with timely and transparent reporting of terms and agreements. At the end of August 2020, China, the largest official creditor, announced that it has reached agreements with half of the 20 low-income countries requesting debt restructuring under the DSSI, marking its first participation in a coordinated, multilateral debt relief initiative. Continued transparency in the lending terms and commitments made by one of the largest lenders in the world would be important in monitoring these efforts and debt sustainability.

Greater coordination should be accompanied by an extension of the DSSI by at least one year (until the end of 2021), generating a further $36 billion in fiscal space. An extension of the policy would give countries time to assess debt sustainability and to define concrete steps towards debt restructuring. Given the net present value of the policy is neutral, insofar as countries will have to repay their full debt requirements (including accrued interests), an extension of this sort would be easily implementable – and would be at a low cost to creditors. In addition to extending the DSSI in time, the G20 should consider whether to expand the initiative in scope and include middle-income countries that are equally liquidity-constrained and limited in financing options.

Nevertheless, it is important to recognise that debt suspension – while the preferred policy option for creditors – simply postpones debt repayments to the future. True debt relief should be the gold standard for vulnerable countries facing unsustainable debt burdens. Countries should draw inspiration from the Heavily Indebted Poor Countries (HIPC) Initiative and related Multilateral Debt Relief Initiative (MDRI), which have collectively relieved more than $100 billion in debt for 37 participating countries.

Admittedly, the structure of debt for low-income countries is much more complex today, due to higher involvement from non-Paris Club and private creditors. Of past HIPC funding, 44 per cent originated from IMF resources and other multilateral institutions, with bilateral creditors financing the remainder. Meaningful debt relief will be complex and take time. It will be important the mechanism is seen as providing equitable treatment across countries and the private sector buys in prior to the roll out of the initiative. Moreover, recipient countries should have access to legal support to navigate the complexities of receiving debt relief. Even if it is not yet time to act, it is time to put in the place the steps for establishing this option.

26 Here, we define official lending as lending that is extended by the government and state-owned entities. China and its subsidiaries have already lent $1.5 trillion to more than 150 countries worldwide. See Sebastian Horn, Carmen Reinhart and Christoph Trebesch, “China’s Overseas Lending,” NBER Working Paper No. 26050 (May 2020), https://www.nber.org/papers/w26050
27 Camilla Hodgson, “China strikes debt deals with poor nations under G20 scheme,” Financial Times, August 30, 2020, https://www.ft.com/content/6900c595-151b-4cfd-90bb-0be9967b7999
28 50 per cent of China’s lending between 1949 and 2017 were not reported to the IMF or the World Bank (Horn et al., 2020). It still remains unclear the extent to which China has committed to DSSI.
In the interim, debt standstill is a necessary first step that would give creditors and debtors the breathing room to assess individual country needs.

**Option 4. Leverage differential pricing to improve the terms of lending and provide more concessional financing**

**Key takeaway:** Differential pricing should be leveraged to improve lending terms for low- and lower-middle income countries. While this option may not generate the same magnitude of funding as the other options, it is an important step towards building a sustainable international financial system.

Of the financing flows, 95 per cent have taken the form of loans (as opposed to grants), raising the likelihood of further debt distress. As a result, the allocation of funding remains inequitable, with funding seemingly directed towards those countries that traditionally receive financing and have a higher capacity to repay the loans, rather than prioritising countries where poverty is skyrocketing. Countries where it is expected that poverty will increase the least as a result of COVID-19 have received US$93 per capita compared to US$26 per capita in countries where poverty is expected to increase the most – and these calculations exclude high-income countries. In a first best scenario, additional financing should take the form of grants. As a second best alternative, it should be easier for low- and middle-income countries to borrow during this crisis.

Differential pricing should be used to better utilise the assets of MDBs. Unlike traditional financing, lending terms should be based on a country’s income status, rather than creditworthiness. For instance, improved lending terms can be achieved through differential pricing of the World Bank’s International Bank for Reconstruction and Development (IBRD) loans to finance highly concessional loans to LICs. With lending based on per capita income, higher income countries pay more and generate additional revenues to subsidise lower-income countries with greater needs. In the current structure of lending across many IFIs, low-income countries, such as Malawi, borrow on concessional terms. These lending rates are much lower than those for lower-middle income countries, such as Bangladesh, where borrowing rates are the same as for upper-middle income countries, such as China and Brazil.

There is scope to adopt differential pricing and subsidise more loans for low-income and even lower-middle income countries. In an important step towards this direction, the Bank’s shareholders have agreed to increase the borrowing costs for upper-middle income countries that are close to graduating, albeit marginally. This agreement reduces the subsidy they (still) benefit from, due to the spread between the IBRD loan and loans obtained on the private market, while raising additional revenue. With lower transaction costs, IBRD lending to upper-middle income countries of this nature – many of whom are already donors (such as China and Brazil) – generates net income or profit for the Bank. In 2018, a price differentiating initiative generated $100 million of additional financing, which was redirected towards financing global public goods.

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31 Centre for Disaster Protection, “COVID-19: Tracking global ODA flows to meet crisis needs,” (26 June 2020), https://static1.squarespace.com/static/5c9d3c35ab1a62515124d7e9/t/5ef5ee03460edc7c455d3a5c/1593175559641/covid19+finanical+tracking+june++26.pdf
32 Ruth Hill, Dillan Patel and Michèle Plichta, “What have we learned after six months of tracking covid-19 funding? We don’t just need more money, we need a different approach.” Centre for Disaster Protection (9 October 2020), https://www.disasterprotection.org/latest-news/what-have-we-learned-after-six-months-of-tracking-covid-19-funding
35 Nancy Birdsall, ibid.
Moreover, to bridge the gap in the system between concessional IBRD and market rates, “frontier” economies transitioning from low-income to lower-middle income status could be offered slightly-below-market financing. Borrowing countries emerging from the IMF and the World Bank financing programmes currently look to the market for unconditional financing, but they pay substantially more. Given greater investor risk aversion, blended financing options for these transitional economies must be developed, as more countries move up the income ladder.36

The introduction of the principle of differential pricing was a major breakthrough, politically and ideologically, even if the actual price differentiation and net income generated remain modest. Nevertheless, this option presents an example of a more sustainable financing framework that avoids a reliance on donor pledges and could be useful for both short-term humanitarian financing and longer-term projects.

Conclusions

It is time to act boldly, and to rewrite the global financial rulebook to respond to this once-in-a-generation crisis. We outline four options for how IFIs and their member states can better leverage their existing capital through more balance sheet optimization and global coordination. In the first best instance, increased capital contributions of member states to multilateral development banks (MDBs) (or recapitalization) would increase their capacity to inject the required liquidity for overcoming this global challenge. This is not an unprecedented option, in light of the $7.5billion capital increase to the World Bank’s IBRD in 2018 to fund “global public goods”, such as pandemic and climate financing.37

However, in the interim, existing capital and relationships can be better leveraged. The four proposed options to expand the support to low- and lower middle-income countries are technically feasible and non-mutually exclusive. They can and should be implemented in tandem.

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