Policy Roundtable on Special Drawing Rights (SDR)

Summary

The *Intergovernmental Group of Twenty-Four (The G-24)* and the *Center for Global Development (CGD)* organized a virtual Roundtable on Special Drawing Rights (SDR). The Roundtable was chaired by Iyabo Masha, Director of the G-24, and moderated by Mark Plant, COO of CGD. Panelists and attendees included scholars, experts, central bank and ministry of finance officials, IMF and World Bank staff and executive directors or alternates, and other practitioners. The discussion was held under Chatham House rules.

Special Drawing Rights were established in 1969 to enhance global liquidity by supplementing countries' official reserves. Over time, they have evolved into an international reserve asset used for various purposes. A 2023 IMF ex-post assessment indicates that members utilized the SDR allocation of 2021 to increase foreign reserves, finance fiscal needs, or a combination of both. While the current use of SDRs has surpassed initial objectives, a number of challenges hinder their potential to further support the global financial safety net and development financing. These challenges include the limited size of SDR allocations, the allocation system which does not consider individual countries' needs, and mixed success with recycling initiatives, especially rechanneling for hybrid capital. The Roundtable reflected on the evolving role of SDRs and explored pathways to enhance their effectiveness in addressing global financial and development challenges. The focus was on harnessing the power of SDRs while ensuring that their benefits are equally distributed; reimagining SDRs to meet today's challenges and overcoming the political and technical hurdles to achieve meaningful results.

ROUNDTABLE DISCUSSIONS

SDR Allocation

A central topic of the discussion was that though SDRs provide a source of financing for many countries, reducing financial vulnerability during crises, they are underutilized. One factor contributing to this is the quota-based formula for SDR allocations, which results in high-income nations accumulating SDRs, while developing countries with significant balance of payments needs for development and climate financing deplete their SDRs. The disparity in holdings and their utility suggests the need for reforms in the allocation framework, quota rebalancing favoring emerging markets and developing countries, and more predictability in future distributions. Panelists suggested that regular SDR allocations would supplement global liquidity, enhancing global trade and economic demand across different income levels, with some advocating for an annual allocation of at least $200 billion. Additionally, it was proposed that a special allocation to developing countries with the greatest needs would address the uneven distribution of SDRs while providing additional resources for sustainable development and financial goals. Panelists also acknowledged the political challenges in building consensus on such an allocation, as well as in amending the IMF Articles of Agreement to alter the existing framework, which requires 85 percent majority at the IMF Executive Board

Recycling SDRs through Multilateral Development Banks

A significant part of the discussion focused on the proposal to recycle SDRs through MDBs in the form of hybrid capital, a move that could amplify their impact by leveraging them up to four times their nominal value in development financing. Panelists highlighted central bank intransigence on the reserve asset status of SDRs as the primary obstacle to advancing SDR rechanneling efforts. But some noted that France's plan to support the process by issuing a guarantee via a liquidity support agreement that will backstop the SDR on-lending at MDBs was as a positive development. Panelists proposed that building coalitions of sympathetic central banks and finance ministries to press the political and technical case for SDRs recycling could be effective. The importance of MDBs participating in the Voluntary Trading Arrangement (VTA) was also underscored by speakers, since that would avoid penalties for countries allocating SDRs to MDBs. Engaging with central banks and the IMF to reform SDR accounting frameworks emerged as a critical action item. Direct allocation of SDRs to MDBs should be considered.

Enhancing the Utilization of Existing Facilities

In addition to advocating for new allocations and recycling, various experts suggested that current arrangements within the IMF, which involve SDR rechanneling through facilities from the Resilience and Sustainability Trust (RST) and the Poverty Reduction and Growth Trust (PRGT), could be optimized. The improvement should aim to increase financing accessibility for countries in need. These facilities have encountered obstacles, including slow disbursement rates, limited flexibility in using RST funds for budget support and operational expenditures, and the necessity for additional subsidy contributions to the accounts. As such, enhancing their functionality is viewed as an immediate and pragmatic approach to maximizing the impact of SDRs.

Innovative Reforms

Some panelists discussed innovative reforms that could better align Special Drawing Rights (SDR) usage with the original intent. Suggestions included creating a separate class of SDRs for developing countries with reduced conditionality or delinking new issuances from the current quota formula, particularly if quota reform continues to be delayed. Another proposal was to utilize SDRs for debt buybacks and restructuring by establishing a "buyer of last resort" mechanism. This approach could finance necessary debt reductions without endangering the solvency of multilateral development banks and would require only minor accounting adjustments.

Additionally, one suggestion aimed at addressing both the adequacy and equality of global liquidity provision advocated for transforming the SDR into a global reserve currency, in alignment with the IMF's mandate under the Articles of Agreement (IMF 1944, Article VIII, Section 7). The potential use of SDRs for liquidity could also pave the way for their application in private sector capital initiatives. For instance, a liquidity sustainability facility could be developed to enhance capital and augment private flows, facilitating the use of SDRs for liquidity purposes.

Institutional and Political Challenges

Panelists acknowledged the complexity of reforming the SDR due to institutional and political constraints, especially the requirement for broad consensus among International Monetary Fund (IMF) member countries. The role of the United States is particularly crucial because of its veto power and the necessity for legislative action in its domestic process. Some were of the view that while recommendations on new allocations and delinking new SDR issuances from the current quota formula may be attractive, political realities present significant challenges, necessitating caution in exploring new allocations to avoid political backlash. Additionally, pre-existing constraints on the SDR and the substantial support required to implement reforms that would enhance the SDR's role make it unlikely that ambitious goals for this "quasi-currency" will be achieved. Instead, a focus on rechanneling SDRs, addressing the challenges posed by the current rules governing SDR usage by central banks, replenishing the subsidy account of the Poverty Reduction and Growth Trust (PRGT), and scaling up the Resilience and Sustainability Trust (RST) holds more promise than fresh SDR allocations. Panelists emphasized the importance of advocacy efforts aimed at changing political perspectives, including engagement with legislators, civil society organizations, and financial institutions to influence key decision-makers.

To advance these efforts, the roundtable outlined some action items which include maintaining ongoing dialogue with central banks to amend SDR rules, mobilizing support for MDB recycling. Additionally, the discussion highlighted the importance of public-private partnerships in enhancing the SDR framework, especially through collaboration with investment funds and philanthropic organizations that can help mobilize additional resources.

Looking ahead, participants stressed the need for a follow-up roundtable to assess progress on these issues, including tracking commitments made by governments and MDBs. The conversation concluded with a call for continued advocacy and research, recognizing that long-term reforms will require sustained effort and collaboration among all stakeholders involved in global finance.

Panelists

Amar Bhattacharya, Senior Fellow, Global Economy and Development Program, Brookings Institution

Andres Arauz, Senior Research Fellow, Center for Economic and Policy Research

Carlo Sdralevich, Division Chief, Finance Department, IMF

Didier Jacobs, Debt Relief Advocacy Lead; Oxfam International

Edwin Truman, Former US Federal Reserve

Francisco Rodriguez, Professor of Practice of International and Public Affairs, University of Dever

Gustavo De Rosa, General Manager of the Finance Department & Chief Financial Officer, Inter-American Development Bank

Hassatou N'Sele, Vice President, African Development Bank Group

Iyabo Masha, Director, The Intergovernmental Group of Twenty-Four (The G24)

Kevin Gallagher, Director, Boston University Global Development Policy Center

Mark Plant, Senior Policy Fellow and Chief Operating Officer, CGD

Pepukaye Bardouille, Director of Bridgetown Initiative and Special Adviser on Climate Resilience, Barbados Prime Minister's Office

Richard Samans, Chair of UN Economist Network Working Group on Human-Centered Economics and Sustainable Development; UN-DESA

Sara Harcourt, Senior Policy Director, Development Finance; ONE Campaign

Stephen Paduano, London School of Economics and Political Science; *IDEAS associate; former US Treasury official.*