May 19, 2021

International Monetary Fund: Special Drawing Rights Allocation

Special Drawing Rights (SDRs) are international reserve assets created by the International Monetary Fund (IMF) to supplement member countries' official foreign exchange reserves. In response to the health and economic effects of the Coronavirus Disease 2019 (COVID-19) pandemic, the G-20 finance ministers in April 2021 announced their support for an SDR allocation worth approximately $650 billion. (While the IMF has not announced an exact number, an allocation of such size would be approximately SDR 448.5 billion).

This would be the first such allocation since the global financial crisis of 2008-2009. Some Members of Congress have sponsored legislation calling for a substantially larger SDR allocation (H.R. 986; S. 67). Other Members have expressed concerns about the SDR allocation and sponsored legislation to strengthen congressional oversight and authority over U.S. support for SDR increases (H.R. 1513; H.R. 1568).

Background on SDRs

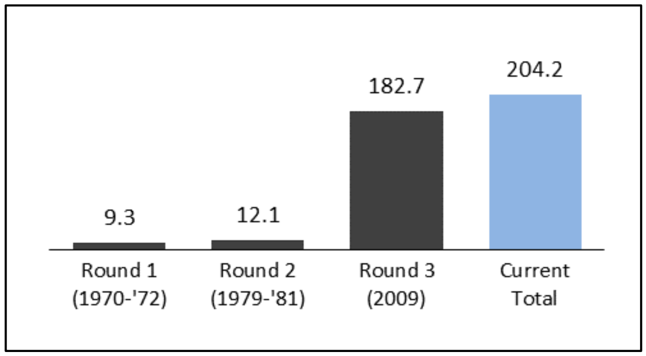
Central banks and other monetary authorities use international reserve assets to: (1) supplement domestic holdings of foreign exchange reserves; (2) meet domestic demand for foreign currency; and (3) assist in maintaining the external value of a domestic currency. The IMF created SDRs in 1969 as a way to bolster members' reserve holdings: SDRs can be exchanged among IMF members for hard currency and used in international transactions by central banks and other monetary authorities. IMF member countries, as well as some 15 international organizations such as the European Central Bank, the Bank for International Settlements, and the International Fund for Agriculture and Development, are able to buy and sell SDRs. Private investors and firms are not permitted to engage in SDR transactions.

SDRs derive their value from the fact that IMF member countries are willing to hold them and exchange them for hard currency. A former IMF general counsel, Francois Gianviti compared the SDR to play money: "The difference is that… the 'play money' can be used to buy real assets and discharge real liabilities and, at the end, real value must be returned if the allocated SDRs have been spent."

The value of SDRs fluctuates with the value of the currencies in its basket. Since 2016, the SDR is equal to the exchange value of a weighted basket of five currencies: the U.S. dollar, the Chinese renminbi, the European euro, the Japanese yen, and the British pound sterling. As of May 18, 2021, one SDR equals U.S. $1.44. When an IMF member exchanges their SDR holdings to another IMF member for hard currency, interest is applied. IMF members receive interest on their SDR holdings and pay charges on their total allocations of SDRs at the same interest rate. The SDR interest rate is a weighted average of 3-month sovereign bill rates of these currencies. The composition of the SDR basket is reviewed every five years, and was next scheduled to be reviewed by September 30, 2021. In March 2021, IMF members agreed to postpone the review until 2022 due to the ongoing discussions about a new SDR allocation.

While the SDR was agreed in principle in 1967, it was not initiated until 1969 after the U.S. passage of the Special Drawing Rights Act of 1968 (22 C.F.R. § 286n). To date, there have been four rounds of allocations, the most recent in 2009, totaling SDR 204.20 billion (approximately $294 billion).

Figure 1. IMF SDR Allocations (To Date)
(SDR billions)



Source: International Monetary Fund.

SDRs are a small percentage of global foreign reserves. Total currency reserves were $12.70 trillion at the end of 2020. Of the countries that report the currency composition of their foreign exchange reserves, the U.S. dollar accounts for 59% of the total. By contrast, SDR allocations total about $294 billion, around 2% of total foreign exchange reserves. This is similar to the proportion of global foreign exchange reserves held in Canadian dollars or Australian dollars. The creation, allocation, and usage of SDRs is separate from the IMF's lending resources According to the rules governing SDRs, SDRs belong to the countries holding them and not to the IMF.

COVID-19 Crisis Response & U.S. Policy

Ensuring developing countries' access to hard currency has been a priority for international economic policy makers throughout the COVID-19 pandemic. While advanced economies have been able to access central bank swap arrangements with the Federal Reserve, European Central Bank, and other major central banks, low-income and developing countries have fewer available options.

Several policymakers, analysts, and non-profit organizations have called for a new allocation of SDRs to increase developing countries' access to hard currency. For example, Jubilee USA, a non-profit financial reform organization, called for a $3 trillion SDR allocation in February 2020. Legislation introduced in April 2020 would have, among other things, instructed the U.S. Treasury to support a $3 trillion SDR allocation (116th Congress, H.R. 6581).

Due to the IMF's voting rules and the substantial U.S. voting share at the IMF, U.S. support is required for a new SDR allocation. During the Trump Administration, Treasury Secretary Steven Mnuchin opposed a new SDR allocation, arguing that only a small portion of the SDRs would go to low-income countries. Additionally, policymakers raised concerns about a new SDR allocation providing funds to China, which already holds sizeable foreign exchange reserves, and providing funding opportunities for countries subject to U.S. sanctions.

The U.S. position shifted under the Biden Administration. In February 2021 Treasury Secretary Janet Yellen announced support for a new SDR allocation. In March 2021, the G-7 endorsed a "new and sizable" allocation of SDRs, and the IMF Executive Directors discussed an SDR allocation of $650 billion. At current exchange rates, this would be approximately SDR 448.5 billion, increasing the amount of IMF SDRs allocated to IMF member counties from SDR 204.2 billion to approximately SDR 652.6 billion.

The G-20 announced its support for an SDR allocation in April 2021. The Treasury Department has linked its support for the SDR allocation with measures to increase transparency surrounding SDR transactions. It is also working on ways for advanced countries to lend a portion of their SDRs in support initiatives targeting low-income countries.

Such an allocation would likely have a substantial impact in low-income countries. According to one analysis by the Peterson Institute for International Economics's Maurice Obstfeld and Harvard Kennedy School's Edwin Truman, 4.5% of a $650 billion SDR allocation ($29.2 billion) would go to low-income countries that are eligible to borrow from the World Bank's International Development Association (IDA). This amount would exceed average annual IDA disbursements during the past three years ($17.8 billion) by more than 60%.

The Role of Congress and Congressional Debate

The Special Drawing Rights Act of 1968 (22 C.F.R. § 286n) sets forth the procedures for U.S. participation in the IMF's SDR Department, among other things. Under the SDR Act, Congress has authorized Treasury to support an SDR allocation without additional legislation under two conditions:

1. The amount allocated to the United States does not exceed U.S. quota in the IMF (currently $119.50 billion) during a five-year period; and
2. The Treasury Department meets specific congressional notification requirements ninety days prior to the SDR allocation.

Under the proposed $650 billion SDR increase, the United States would be allocated $113.36 billion of SDRs (based on a U.S. quota share of 17.44% of total quotas). Thus, the proposed $650 billion SDR allocation would be below the threshold that would require congressional authorization.

On April 1, 2021, the Treasury Department formally notified Congress of its plans for the new allocation, starting the 90-day congressionally mandated consultation process, which would be completed in early July.

As noted above, some Members of Congress have sponsored legislation calling for an SDR allocation of at least $2 trillion (H.R. 986; S. 67)—substantially larger than the proposed SDR allocation. Advocates argue that, unlike other measures, such as a full IMF quota increase, SDR allocations are able to be implemented quickly and benefit a larger number of developing countries.

Other Members have introduced legislation to require or strengthen congressional authorization for U.S. support of an SDR allocation (H.R. 1513; H.R. 1568). Skeptics have raised concerns about the transparency, accountability, and effectiveness of a new SDR allocation. Additionally, concerns have been raised about potential risks to U.S. taxpayers and whether a new SDR allocation might increase financial support to countries subject to U.S. financial sanctions, such as Iran and Venezuela.

Select Policy Questions for Congress

- Is the current threshold triggering congressional authorization for U.S. support of an SDR allocation optimal? What is the trade-off between granting the Administration flexibility during crises and safeguarding congressional role in formulating U.S. IMF policy?
- How helpful was the SDR allocation during the global financial crisis of 2008-2009? In what ways is that financial crisis relevant to the economic crisis triggered by the pandemic?
- How are negotiations to improve the transparency of SDR transactions proceeding? What information about SDR transactions should be public?
- What is the IMF policy on SDR transactions involving countries subject to sanctions?
- What are the Administration's plans, if any, for pursuing another SDR allocation when the new five-year SDR period begins in 2022?
- What are the options for leveraging a portion of some countries' SDRs to support low-income countries? What is China's interest in participating in such initiatives?

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