

# NEW ALLOCATION OF SPECIAL DRAWING RIGHTS

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BANCO DE ESPAÑA

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## Abstract

In August 2021, the International Monetary Fund (IMF) made a new allocation of Special Drawing Rights (SDRs) equivalent to \$650 billion. This significant amount has tripled the total existing stock of SDRs. For Spain it involves an increase of 16% in foreign reserves, and an increase in receivables from the IMF, which amount to 22% of the reserves on the balance sheet of the Banco de España, as compared with 10% at present.

The purpose of this expansion of SDRs is to support a group of countries that are having most difficulty fighting the impact of the COVID-19 pandemic. These countries have a greater need for foreign exchange to obtain basic supplies just when they are shut out of international capital markets. The new allocation is likely to boost SDR transactions given its large amount, the urgent need for funds in some countries and the experience of the 2009 allocation.

This paper explains the characteristics of the use of SDRs as an effective source of liquidity, concluding that the way in which the issuance of this instrument is made effective is by means of transactions, allocation being the formal prerequisite for their existence. Accordingly, the key to their effectiveness will be the transactions actually carried out to obtain liquidity in international business. A liquidity ratio is proposed for monitoring their use. With regard to the magnitude of the allocation and, given that it is based on the quotas of each IMF member country, the developed countries have received the bulk of the allocation, as opposed to those countries having greater difficulty accessing the markets. Accordingly, measures will have to be taken to promote the passing on of SDRs so that their purpose can be achieved and they effectively supplement the reserves available within the framework of international trade.

**Keywords:** SDRs, allocation, IMF, COVID-19, pandemic, liquidity, reserve assets, foreign exchange, voluntary trading arrangements, international cooperation.

**JEL classification:** F33, F42, G15.

## Resumen

El Fondo Monetario Internacional (FMI) realizó en agosto de 2021 una nueva asignación de derechos especiales de giro (DEG), por un importe equivalente a 650 mm de dólares estadounidenses. Se trata de una cuantía significativa, que triplica los saldos actuales. En particular, para España ha supuesto un incremento de un 16 % de las reservas exteriores, así como de los activos frente al FMI, que alcanzarían un 22 % de las reservas en el balance del Banco de España, en comparación con el 10 % actual.

El objetivo de esta expansión de los DEG es dar apoyo a un grupo de países con mayores dificultades para combatir el impacto de la pandemia de COVID-19, a lo que se ha unido una mayor necesidad de divisas para obtener suministros básicos, con un cierre de los mercados de capitales internacionales. Es previsible que la nueva asignación dinamice la operativa en DEG, dados su elevado importe, la acuciante necesidad de fondos en algunos países y el aprendizaje respecto a la asignación de 2009.

En este documento se explican las características del uso de los DEG como fuente efectiva de liquidez, con la conclusión de que el modo en que se hace efectiva la emisión de este instrumento es mediante las transacciones, y de que es la asignación el presupuesto formal de su existencia. Por tanto, el aspecto clave para su efectividad será la realidad de las transacciones que se hagan para obtener liquidez en el tráfico internacional. Con el objetivo de hacer un seguimiento de su uso, se sugiere una ratio de su liquidez. Por otro lado, en relación con la magnitud de la asignación, y puesto que se realiza en función de las cuotas de cada país miembro del FMI, se observa un «acaparamiento» por parte de los países desarrollados, frente a los que muestran más dificultades en el acceso a los mercados, que hará inevitable la adopción de medidas que favorezcan la recirculación de los DEG para alcanzar sus fines, de modo que se complementen eficazmente las reservas disponibles en el marco del comercio internacional.

**Palabras clave:** DEG, asignación, FMI, COVID-19, pandemia, liquidez, activos de reserva, divisas, acuerdos de canje voluntario, cooperación internacional.

**Códigos JEL:** F33, F42, G15.

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## 1 Proposal for a new SDR issue

Special Drawing Rights were created by the IMF in 1969 to supplement the available official reserves.<sup>1</sup> SDRs are high quality reserves, on a par with gold, the US dollar and the euro, their use is unconditional and they are not subject to maturity. As international reserve assets they have certain special features: they are an instrument for monetary cooperation between countries, coordinated by the IMF; they act as a unit of account for transactions between the IMF and its member countries; and their use also extends to certain international organisations.<sup>2</sup> However, they cannot be considered a currency in the conventional sense, since they can only be used and traded by certain agents, member countries and certain international and regional institutions and they cannot be used by private institutions or individuals. Lastly, their value is determined by a basket of five major international currencies<sup>3</sup> (see Box 1).

The COVID-19 pandemic has led to an economic slump without precedent since the Great Depression, especially in the developing countries, Sub-Saharan Africa, Latin America and the Caribbean. These countries are suffering from a shortage of currency reserves just when they need them most, with grave consequences from a humanitarian standpoint. In this setting, both the International Monetary and Financial Committee (IMFC)<sup>4</sup> and the Managing Director of the IMF published a proposal<sup>5</sup> for a new SDR allocation in an amount equivalent to \$650 billion. At the same time, certain European<sup>6</sup> and African leaders also called on the IMF to make this new allocation. The Executive Board approved the Managing Director's proposal on 8 July. In early August it was approved by the Board of Governors,<sup>7</sup> and the allocation became effective at the end of that month.<sup>8</sup>

In 2009, against the backdrop of the international financial crisis, the then largest allocation of all time was made, in an amount of SDR 161 billion.<sup>9</sup> The 2021 expansion amounts to SDR 456 billion,<sup>10</sup> almost three times the amount issued in 2009. As a total amount of

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1 A country's reserve assets are those foreign assets that the monetary authority has under its control and available for its use.

2 By way of example, the Bank for International Settlements (BIS) issues its annual accounts in SDRs. Also, certain treaties, for instance the Convention for the Unification of Certain Rules for International Carriage by Air, signed in Montreal in 1999, contain references to amounts in SDRs.

3 The US dollar, euro, pound sterling, Japanese yen and Chinese renminbi.

4 The IMFC advises the IMF Board of Governors and determines the strategic direction of the IMF, guiding the Executive Board.

5 Both proposals, that of the IMFC and that of the Managing Director, were published for the IMF Spring Meetings, 5-11 April 2021.

6 Giuseppe Conte, Italy; António Costa, Portugal; Ursula von der Leyen, President of the European Commission; Emmanuel Macron, France; Angela Merkel, Germany; Charles Michel, President of the European Council; Mark Rutte, the Netherlands; Pedro Sánchez, Spain. Other public figures, such as Gordon Brown (former British Prime Minister) and Larry Summers (former US Secretary of the Treasury), have also called for the issuance of SDRs.

7 The Board of Governors is the highest decision-making body of the IMF. While it has delegated many of its powers to the Executive Board, it retains the right to approve quota decisions, SDR allocations and amendments to the Articles of Agreement. With regard to the governance of relations between the Spanish State and the IMF, the Spanish Government participates in the Board of Governors through the relevant minister and has the voting rights, while the Governor of the Banco de España is the alternate governor on the IMF Board of Governors.

8 New allocations must become effective 21 days after their approval by the Board of Governors. Since the new allocation was approved on 2 August, it became effective on 23 August.

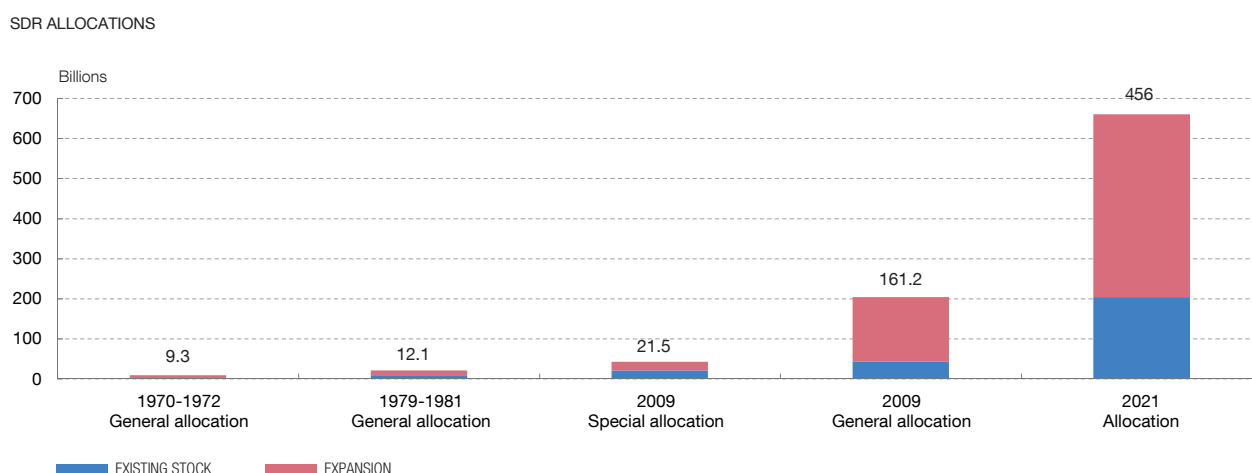
9 In 2009, a special one-time allocation of SDR 21.5 billion was made to restore the balance between SDR allocations and quotas, compensating those countries that had "missed out" on previous allocations, having joined the IMF after 1981.

10 On 1 July, when the allocation was discussed by the Executive Board, the exchange rate stood at SDR 0.702283/USD.



Chart 1  
SDR ALLOCATIONS

With the latest allocation a total of SDR 660.7 billion has been reached.



SOURCE: IMF.

SDR 204 billion had been allocated up to 2021, this new proposal takes the total volume allocated to SDR 661 billion (see Chart 1).

The new SDR issue (\$650 billion) is the highest amount legally possible in the United States without requiring approval by Congress. It is important to note that, in order for these proposals to be successful, the US Administration plays a decisive role, as the United States has a de facto right of veto over these decisions.<sup>11</sup> Indeed, the new Administration has smoothed the path for approval of the issue, as its backing was essential, given that, in accordance with the IMF's Articles of Agreement, the Managing Director can only submit proposals for new allocations for approval when the necessary support is guaranteed.

There was broad debate on the question of the amount of funds to be placed at the disposal of the countries most in need. SDR allocations are made in accordance with quotas, which means that, in absolute terms, the bulk of the allocations are made to the more developed countries, which are not those targeted by this measure. For instance, the United States and the euro area countries account for 40% of the quotas, and thus receive allocations in that proportion (Table 1 shows the amounts allocated to a range of countries in the new allocation). These more developed countries already have in place their own programmes to combat the effects of the pandemic<sup>12</sup> and they are less likely to need to use the allocation.

<sup>11</sup> The United States has 16.51% of the votes. As these decisions require a vote in favour of at least 85%, it has a de facto right of veto.

<sup>12</sup> In the euro area the Pandemic Emergency Purchase Programme (PEPP) has an envelope of €1.85 trillion. This is in addition to the Next Generation EU (NGEU) funds (€750 billion) and the European instrument for temporary Support to mitigate Unemployment Risks in an Emergency (SURE) (€100 billion).

Table 1

**AMOUNT OBTAINED IN 2021 ALLOCATION (a). EUROPE AND AMERICAS**

The table shows the amount of SDRs actually allocated, rounded to the nearest million. As a benchmark, each country's quota is also shown.

SDR million

|                     | Quota (b)  | New allocation |                | Quota (b)   | New allocation |
|---------------------|------------|----------------|----------------|-------------|----------------|
| United States       | 17.4       | 79,546         | Germany        | 5.6         | 25,528         |
| Canada              | 2.3        | 10,566         | France         | 4.2         | 19,318         |
| Brazil              | 2.3        | 10,583         | United Kingdom | 4.2         | 19,318         |
| Mexico              | 1.9        | 8,542          | Italy          | 3.2         | 14,444         |
| Venezuela           | 0.8        | 3,568          | Spain          | 2.0         | 9,139          |
| Argentina           | 0.7        | 3,055          | Netherlands    | 1.8         | 8,374          |
| Colombia            | 0.4        | 1,960          | Belgium        | 1.4         | 6,144          |
| Chile               | 0.4        | 1,672          | Switzerland    | 1.2         | 5,531          |
| Peru                | 0.3        | 1,279          | Sweden         | 0.9         | 4,246          |
| Ecuador             | 0.2        | 669            | Poland         | 0.9         | 3,925          |
| Dominican Republic  | 0.1        | 458            | Austria        | 0.8         | 3,769          |
| Trinidad and Tobago | 0.1        | 450            | Norway         | 0.8         | 3,599          |
| Guatemala           | 0.1        | 411            | Ireland        | 0.7         | 3,307          |
| Uruguay             | 0.1        | 411            | Denmark        | 0.7         | 3,297          |
| Jamaica             | 0.1        | 367            | Greece         | 0.5         | 2,328          |
| Panama              | 0.1        | 361            | Finland        | 0.5         | 2,310          |
| Costa Rica          | 0.1        | 354            | Czech Republic | 0.5         | 2,090          |
| El Salvador         | 0.1        | 275            | Portugal       | 0.4         | 1,975          |
| Nicaragua           | 0.1        | 249            | Hungary        | 0.4         | 1,859          |
| Honduras            | 0.1        | 239            | Romania        | 0.4         | 1,736          |
| Bolivia             | 0.1        | 230            | Luxembourg     | 0.3         | 1,267          |
| Paraguay            | 0.0        | 193            | Slovakia       | 0.2         | 959            |
| Guyana              | 0.0        | 174            | Bulgaria       | 0.2         | 859            |
| Haiti               | 0.0        | 157            | Croatia        | 0.2         | 688            |
| Surinam             | 0.0        | 124            | Slovenia       | 0.1         | 562            |
| Belize              | 0.0        | 26             | Lithuania      | 0.1         | 423            |
| <b>Total (c)</b>    | <b>7.9</b> | <b>35,807</b>  | Latvia         | 0.1         | 318            |
|                     |            |                | Cyprus         | 0.1         | 291            |
|                     |            |                | Estonia        | 0.1         | 233            |
|                     |            |                | Malta          | 0.0         | 161            |
|                     |            |                | <b>Total</b>   | <b>32.4</b> | <b>147,998</b> |

SOURCE: IMF.

a The 2021 allocation to all IMF members amounted to SDR 456,485 million.

b This is not the quota used for the purpose of allocations as it is adjusted according to the quotas actually paid up by all the countries. Thus, the Spanish quota (2.00%, rounded off) increases to over 2.002%.

c The totals do not include either the United States or Canada. The shaded area refers to the other countries in the region.

Accordingly, given that the declared aim of this new allocation is to provide support to countries that have the most difficulties accessing other programmes, the need to improve the way in which SDRs can be passed on – and reallocated – between member countries has arisen. How this may be done – via donations, loans, contributions to development

banks, etc. – is yet to be determined. Countries may already contribute SDRs to the IMF's Poverty Reduction and Growth Trust (PRGT), a programme that provides financial support to low-income countries (Spain's participation in this programme is explained later in this paper). A new Resilience and Sustainability Trust (RST) is also being studied that will take into consideration member countries' priorities regarding support for a more sustainable recovery from the crisis (in terms of combating climate change).

In any event, this new SDR allocation will provide additional liquidity for countries in need of reserves, as it entails a very significant injection of funds in relative terms, without increasing their debt, and supplements other measures rolled out by the IMF. In order to use the SDR allocation, countries in need of reserves will first need to convert the SDRs into a freely usable currency on the international markets, primarily the US dollar. For that purpose, they must submit a request to the IMF to exchange their SDRs into the chosen currency. The next section describes the procedures in place to convert SDRs into liquid currency.

## 2 SDRs as a source of liquidity

SDRs are placed at countries' disposal by means of an accounting entry on their central banks' balance sheets, with an initial entry of the same amount on both the debit and the credit side. This entry entails an increase in the central bank's balance sheet, but it has no impact on liquidity and produces no initial net increase in assets or liabilities. The way in which SDRs can ultimately generate liquid funds to be used in the economic circuit is described below (see Box 2 on the allocation mechanism).

From the real liquidity standpoint, the key figure is the net SDR position in the financial statements of the IMF's SDR Department, which is responsible for managing SDRs. The SDRs held by the IMF itself and by international organisations amount to a positive net position of SDR 23,675 million,<sup>13</sup> while the positive net SDR position of member countries stands at SDR 7,815 million. The combined position amounts to SDR 31,490 million, which is also the negative net SDR position for those countries whose holdings are below their allocations. As the amount allocated up to April 2021 was SDR 204,162 million, and the net SDR position in the SDR Department's financial statements was SDR 31,490 million (15% of the total allocated at that time), this ratio provides a measure of current SDR liquidity and of the role of each of the agents involved<sup>14</sup> (see Box 4 for a description of this ratio).

Given that the IMF does not receive SDR allocations, its SDR holdings arise from member countries' quotas (which must be subscribed in reserve assets),<sup>15</sup> the payment of charges<sup>16</sup> and loan repayments. The IMF uses these SDRs to pay interest on positive net positions and to grant credit facilities to member countries.

Member countries may use their SDR holdings to obtain freely usable currency – by means of the transactions described in the following paragraph – which can be used to make payments to other agents outside the SDR circuit, pay for imports, make debt repayments in foreign currency, etc. To boost the liquidity and acceptance of SDRs, the IMF does not apply the strict balance of payments need criterion to these transactions, nor does it require that countries' SDR holdings be equivalent to a specific proportion of their allocations.<sup>17</sup>

In addition to being traded<sup>18</sup> to meet member countries' needs, SDRs are also the mandatory currency for collecting interest on holdings and paying charges and in the event

<sup>13</sup> At 30 April 2021, the close of the IMF's fiscal year, the General Resources Account (GRA) Department's position stood at SDR 22,203 million, and that of other authorised institutions at SDR 1,472 million.

<sup>14</sup> This discussion of SDR liquidity does not address the advantage gained from merely holding and having available these reserve assets in terms of boosting confidence in certain economies and lowering the likelihood of crisis. This has been said in some cases to be a factor behind the low level of use of SDRs.

<sup>15</sup> Including SDRs.

<sup>16</sup> In Fund terms, "charges" are the payments made by member countries for the allocations received, while "interest" refers to the amounts received by countries on their SDR holdings. In both cases, the SDR interest rate is used.

<sup>17</sup> The initial obligation to maintain a daily average level per quarter was abolished in 1981. However, limits may currently be established under bilateral ad hoc agreements with the IMF. For example, in the ambit of the Voluntary Trading Arrangements (VTAs), the Spanish VTA sets a range of 65% to 135%. But these ranges are only a reference for the IMF, as the Banco de España can perform operations that exceed these limits, within the VTA governance sphere described later in this paper.

<sup>18</sup> Purchased and repurchased in IMF terminology.

of cancellation of allocations<sup>19</sup> (in this contingency, if the SDRs held are insufficient to meet these payments, they must be obtained in exchange for freely usable currencies). SDRs may also be used for loans, payment of obligations, as pledges, and in IMF operations such as interest payments on loans, loan repayments and quota subscriptions (reserve tranche).

## 2.1 Conversion into freely usable currencies<sup>20</sup>

Most transactions involving SDR holdings consist of the spot purchase and sale of SDRs against freely usable currencies through either of the following two options:

- **Designations:** This mechanism ensures that SDRs can be converted into freely usable currencies if a participating country needs to do so<sup>21</sup> and the voluntary trading arrangements described below have insufficient capacity to absorb sales. It guarantees the liquidity of SDRs and their role as a reserve asset.

Under this mechanism, the IMF can designate a member country with a strong external position to purchase (sell) SDRs from (to) other member countries with a less favourable external position. The country designated by the IMF is obliged to purchase or sell up to 300% of its allocation, although a higher limit may be established with the agreement of the designated country. The IMF will approach countries that have a strong balance of payments and reserve position (this may include countries that have a moderate balance of payments deficit but a high volume of reserves).

The IMF Executive Board draws up an annual designation plan, in case one is needed, in an endeavour to achieve a balanced distribution of SDR holdings. This balance is measured by the excess of SDRs over allocations and official gold and currency holdings. The designation mechanism was last activated in 1987.

- **Voluntary trading arrangements (VTAs)<sup>22</sup>** are arrangements through which a group of countries act as market-makers. These arrangements set conditions, such as the type of currency to be provided and a benchmark range of holdings to be held by countries.

At present, 31 countries, plus the European Central Bank (ECB), have VTAs. The Eurosystem accounts for 16 of this 32-member group, while the 15 euro

<sup>19</sup> This refers to partial cancellation of allocations by the IMF, which is a possibility envisaged in the Articles of Agreement and is also based on the absence of a need to supplement international reserve assets in the long term.

<sup>20</sup> The IMF's Articles of Agreement differentiate between Transactions, which are exchanges between SDRs and other currencies (exchanges of monetary assets), and Operations, which are other uses or receipts of monetary assets by the IMF (use of monetary assets).

<sup>21</sup> Balance of payments need, Article XIX of the Articles of Agreement.

<sup>22</sup> At present there are 32 voluntary SDR trading arrangements in place, including the 19 new arrangements following the 2009 allocation. Spain has had a VTA since 2009.

area countries that have VTAs account for some 22% of the total.<sup>23</sup> In the 2009 allocation these arrangements received a sharp boost, with the inclusion of 19 new countries, to make the above-mentioned total of 32 VTAs. Likewise, with the new allocation, the IMF is seeking to include new countries in these voluntary arrangements.

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<sup>23</sup> The exact figure is 21.64%, while the United States accounts for 17.44%.

### 3 Spain's SDR holdings

Following the description of the general features of the proposed allocation, the nature of SDRs and how they are traded, and how the IMF operates as a supplier of reserves, this section provides some information on Spain's participation.

According to IMF rules, member countries must designate a fiscal agency<sup>24</sup> (the operational interlocutor with the IMF) and a depository<sup>25</sup> (for all the IMF's holdings of the respective country's currency). In most countries, including Spain, the national central bank is designated to perform both functions.<sup>26</sup>

As the IMF is an international organisation engaged in international monetary cooperation,<sup>27</sup> the functions it performs entail no transfer of sovereignty from the member countries.<sup>28</sup> Accordingly, its decisions are not applied directly, but are addressed to each member country which implements them internally in accordance with its own legal system. In practice, in Spain the IMF's decisions are ratified by means of enabling legislation,<sup>29</sup> whereby increases in quotas and loan agreements are ratified and new SDR allocations are accepted. By law<sup>30</sup> the Banco de España is obliged to pay the quota, finance the obligations assumed under loan agreements and record them as assets on its balance sheet. By law it is also authorised to record SDR allocations on its balance sheet, and is required to record these assets and liabilities on its balance sheet. Spain's voting rights in the IMF correspond, by law, to the Government.<sup>31</sup> Under the Law of Autonomy of the Banco de España, the obligations deriving from membership of the IMF are exempt from the prohibition on State financing.

In consequence, the Banco de España's balance sheet reflects claims on the IMF (on the assets side) and the SDRs allocated to Spain (on the liabilities side). The balance sheet is drawn up in euro, so these data reflect the SDRs expressed in euro (see Table 2).

On the assets side of the balance sheet (see Table 3), there are three items related to these operations:

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24 Article V, Section 1 of the IMF's Articles of Agreement and section G-1 of the IMF's By-Laws, Rules and Regulations. The fiscal agency has no relation to tax matters, but acts as the sole channel for financial transactions with the IMF. Depending on the country, it will be the Ministry of Finance, the central bank, an exchange stabilisation fund (as in the United States) or other body.

25 Article XIII, Section 2 of the IMF's Articles of Agreement.

26 For readers interested in the process of Spain's accession to the IMF, see Cavalieri (2014). When Spain first joined the IMF, the now defunct Spanish Foreign Currency Institute (Instituto Español de Moneda Extranjera, IEME) was designated to perform these functions. Subsequently, the 1962 Banking Law designated the Banco de España as its successor in this respect.

27 The purposes of the IMF are described in Article 1 of the Articles of Agreement. The Fund shall be guided by these purposes in all its policies and decisions.

28 Unlike organisations that seek to integrate or unify, such as the European Union, where there is a transfer of Member States' sovereign powers to common EU institutions. Accordingly, higher State functions are assigned to bodies independent of States and certain decisions adopted may have a direct impact on national legal systems.

29 See the Preamble of Law 13/1999 of 21 April 1999 whereby Spain signed up to various IMF agreements.

30 First final provision of Law 13/1999.

31 Article 13.2 of the Law of Autonomy of the Banco de España.

Table 2

**BANCO DE ESPAÑA BALANCE SHEET STATEMENT (a)**

The table shows the foreign reserves data and the net asset and liability position with the IMF.

In millions

|   | In €           | In SDRs (b)    |
|---|----------------|----------------|
| <b>ASSETS</b>   |                |                |
| Gold and gold receivables   | 13,916.0       |                |
| Claims on non-euro area residents denominated in foreign currency | 46,601.0       |                |
| <b>Claims on the IMF</b>  | <b>6,588.0</b> | <b>5,485.0</b> |
| <b>LIABILITIES</b>  |                |                |
| <b>Counterpart of SDRs allocated by the IMF</b>                   | <b>3,396.7</b> | <b>2,828.0</b> |

**SOURCE:** Statistical Bulletin, Banco de España.

**a** At 31 July 2021.

**b** Exchange rate = SDR 0.832570/€.

Table 3

**BREAKDOWN OF CLAIMS ON THE IMF (a)**

The reserve tranche of the quota records the subscriptions paid. The SDR holdings are those arising from allocations and successive SDR operations. The borrowing arrangements refer to claims on the IMF as a result of the funds drawn under those arrangements.

In millions

|                          | In €         | In SDRs (b)  |
|--------------------------|--------------|--------------|
| Reserve tranche of quota | 2,741        | 2,282        |
| SDR holdings             | 3,071        | 2,557        |
| Borrowing arrangements   | 776          | 646          |
| <b>Total</b>             | <b>6,588</b> | <b>5,485</b> |

**SOURCE:** Statistical Bulletin, Banco de España.

**a** At 31 July 2021.

**b** Exchange rate = SDR 0.832570/€.

- The reserve tranche of the quota records the subscriptions paid.<sup>32</sup> These payments may be made against reserves or in euro. This second option is available because the euro is one of the freely usable currencies.<sup>33</sup>
- SDR holdings are those arising from allocations and successive SDR operations (described in more detail later).

<sup>32</sup> Countries pay 25% of their respective quotas in freely usable currencies, while the other 75% is placed at the Fund's disposal in their local currency. This initial 25% is the reserve tranche of the quota; the remainder is the local currency portion.

<sup>33</sup> In the past, before the euro was introduced, the reserve tranche was subscribed in foreign currency or even in gold. The rest of the quota – the 75% payable in local currency – is dubbed the euro portion and is not part of reserves.



Table 4

**SPANISH QUOTA (a)**

Drawings by the IMF against the account in euro at the IMF's disposal (equivalent to the part of the quota not paid in, i.e. the euro portion) require that the reserve tranche and the euro portion be subsequently rebalanced as the quota remains constant.

In millions (b)

|                 | In SDRs | In €   |
|-----------------|---------|--------|
| Spanish quota   | 9,536   | 11,454 |
| Reserve tranche | 2,281   | 2,740  |
| Euro portion    | 7,255   | 8,714  |

**SOURCE:** Banco de España.

**a** At 31 July 2021.

**b** Exchange rate = SDR 0.832570/€.

- Lastly, the assets deriving from amounts provided to the IMF under borrowing arrangements. These are claims on the IMF as a result of funds drawn under the framework of commitments acquired by the Banco de España and other loan agreements.

The amount of these three components is influenced by the currency used in the transactions and operations. Thus, the amount of the SDR holdings is affected by the interest received and paid on the balances and by purchases and sales of SDRs under Spain's VTA. The amount of the reserve tranche is affected by the drawings made against the IMF's account in euro on the liabilities side,<sup>34</sup> since there is no change in the quota.<sup>35</sup> Accordingly, drawings made by the IMF against the part of the quota not paid in, formally in local currency (in the Spanish case, in euro), require that the reserve tranche and the euro portion be subsequently rebalanced,<sup>36</sup> as the quota remains constant.<sup>37</sup>

Drawings are made at the initiative of the IMF. For example, purchases (or sales) of currency by third countries (see Box 3 for an outline of the role of the IMF and its standard operations) or maturities of borrowed funds will affect the reserve tranche (if the drawings or repayments are made in euro) or the amount of SDR holdings (if the payments or repayments are made in SDRs).

<sup>34</sup> The liabilities-side account in euro in the IMF's favour is equivalent to the euro portion of the quota.

<sup>35</sup> There is a formal procedure for changes in quotas, which are made to reflect changes in the variables that affect the calculation formula, including GDP, openness, the variability of capital flows, and levels of reserves. The 16th Quota Review is currently under way, to be concluded in 2023.

<sup>36</sup> For example, as the quota remains constant, if the IMF asks that €1 billion (assuming this is equivalent to SDR 800 million) be provided to a third country against the euro portion, the balance must be restored between the reserve tranche and the euro portion. Accordingly, with the quota at SDR 9,536 million, this entails increasing the reserve tranche by SDR 800 million, and thus reducing the euro portion by the same amount, using the portion of the quota not initially paid in.

<sup>37</sup> Operations involving quotas as the first line of defence to be used by the IMF. This example is based on the standard purchase operation explained in Box 3. It is different from purchases of SDRs (holdings from allocations) in which amounts may also be provided in euro, under the VTA framework, as described in section 2.1.

The singular features of the euro, Spain's legal tender, have two important implications:

- The euro is issued under a monetary union, which requires taking into consideration a coordinated Eurosystem approach. Given that the Eurosystem has a single monetary policy, the ECB is informed of any transactions that entail changes in the monetary base so as to facilitate correct liquidity monitoring.<sup>38</sup> This applies, in particular, to drawings made by the IMF in euro against the euro portion of the Spanish quota.<sup>39</sup> It also applies to IMF-intermediated purchases of euro by third countries against SDRs<sup>40</sup> and their potential repurchase (the inverse transaction). And, lastly, to IMF drawings in euro under the framework of loan commitments and third-country support programmes. Coordination is a legislative mandate: under the Treaty on the Functioning of the European Union (TFEU), policy measures relating to SDR holdings shall be adopted by the Council.<sup>41</sup>
- The euro is not only the legal tender in the countries of the Eurosystem, but also one of the currencies that makes up the SDR basket of currencies. Accordingly, contributions to quota increases may be fully paid in euro, which means that the difference between the reserve tranche and the local currency portion is a time factor, with 25% being paid upon subscription and 75% being placed at the IMF's disposal for future drawings.<sup>42</sup>

### 3.1 SDR holdings on the balance sheet

The SDRs allocated to Spain since 2009 amounted to SDR 2,828 million.<sup>43</sup> This is the account entry on the liabilities side which, technically, remains unchanged once the allocation has been made. Given that Spain has a quota of 2.00% of the total, in the 2021 issue it was allocated SDR 9,139 million (some €10,977 million),<sup>44</sup> making a total of SDR 11,967 million allocated.

The balance available on the assets side of the balance sheet at 31 July 2021 was SDR 2,557 million.<sup>45</sup> Accordingly, following recording of the new allocation (SDR 9,139 million), the total balance stood at SDR 11,696 million; this is less than the total allocations (SDR 11,967 million) as a result of the SDR transactions performed (see

<sup>38</sup> At present, in view of the non-standard monetary policy measures being implemented by the ECB, which currently has a €20 billion asset purchase schedule per month plus reinvestment of principal payments from previous programmes, and the consequent excess liquidity in the system, in principle the need to assess the impact of IMF operations on monetary aggregates is less pressing.

<sup>39</sup> This is equally applicable to any other euro area country.

<sup>40</sup> These operations are described in the section on how the IMF operates.

<sup>41</sup> Article 138.1 of the TFEU: "In order to secure the euro's place in the international monetary system, the Council, on a proposal from the Commission, shall adopt a decision establishing common positions on matters of particular interest for economic and monetary union within the competent international financial institutions and conferences. The Council shall act after consulting the European Central Bank". Also, Articles 127 and 219 of the TFEU and Articles 3 and 6 of the Statute of the European System of Central Banks (ESCB).

<sup>42</sup> The liabilities-side account in euro at the IMF's disposal.

<sup>43</sup> The amount allocated previously was SDR 299 million.

<sup>44</sup> At the exchange rate of 0.832570 at 30 July 2021.

<sup>45</sup> At 31 July 2021.

Table 5

**BANCO DE ESPAÑA BALANCE SHEET FOLLOWING ALLOCATION**

Simulation using data as at 31 July 2021.

| In millions   | In €           | In SDRs        | % (b)     | New allocation  |                | Totals          |                 | % (b)     |
|---|----------------|----------------|-----------|-----------------|----------------|-----------------|-----------------|-----------|
|   |                |                |           | In € (a)        | In SDRs        | In € (a)        | In SDRs         |           |
| <b>ASSETS</b>   |                |                |           |                 |                |                 |                 |           |
| Gold and gold receivables   | 13,916.0       |                |           |                 |                |                 |                 |           |
| Claims on non-euro area residents denominated in foreign currency | 46,601.0       |                |           |                 |                |                 |                 |           |
| <b>Claims on the IMF</b>  | <b>6,588.0</b> | <b>5,485.0</b> | <b>10</b> | <b>10,976.9</b> | <b>9,139.0</b> | <b>17,564.9</b> | <b>14,624.0</b> | <b>22</b> |
| <b>LIABILITIES</b>  |                |                |           |                 |                |                 |                 |           |
| <b>Counterpart of SDRs allocated by the IMF</b>                   | <b>3,396.7</b> | <b>2,828.0</b> |           | <b>10,976.9</b> | <b>9,139.0</b> | <b>14,373.6</b> | <b>11,967.0</b> |           |

**SOURCE:** Statistical Bulletin, Banco de España.**a** Exchange rate = SDR 0.832570/€.**b** Claims on the IMF as a percentage of foreign reserves.

Table 6

**BREAKDOWN OF CLAIMS ON THE IMF, INCLUDING THE ALLOCATION (a)**

The new allocation increases the SDR holdings item.

| In millions              | % (b)        |              | New allocation |              | Totals        |               |
|--------------------------|--------------|--------------|----------------|--------------|---------------|---------------|
|                          | In €         | In SDRs      | In €           | In SDRs      | In €          | In SDRs       |
| Reserve tranche of quota | 2,741        | 2,282        |                |              | 2,741         | 2,282         |
| SDR holdings             | 3,071        | 2,557        | 10,977         | 9,139        | 14,048        | 11,696        |
| Borrowing arrangements   | 776          | 646          |                |              | 776           | 646           |
| <b>Total</b>             | <b>6,588</b> | <b>5,485</b> | <b>10,977</b>  | <b>9,139</b> | <b>17,565</b> | <b>14,624</b> |

**SOURCE:** Statistical Bulletin, Banco de España.**a** At 31 July 2021.**b** Exchange rate = SDR 0.832570/€.

Chart 2). In consequence, in terms of SDR holdings, Spain has a negative net SDR position.<sup>46</sup> Nevertheless, it has other claims<sup>47</sup> on the IMF which exceed that negative amount.

In July, the Banco de España's total reserves amounted to €67,105 million,<sup>48</sup> including the claims on the IMF<sup>49</sup> which accounted for 10% of total reserves. Following the new allocation, the SDR holdings amount to SDR 11,696 million<sup>50</sup> (approximately €14,048 million). The claims on the IMF<sup>51</sup> thus account for 22% of total reserves<sup>52</sup> (see Table 5).

<sup>46</sup> In the SDR Department's financial statements.<sup>47</sup> Loans to the IMF in generic terms.<sup>48</sup> Including €13,916 million in gold reserves.<sup>49</sup> €6,588 million.<sup>50</sup> The result of adding the SDR holdings at 31/07/2021 (SDR 2,557 million) to the new SDR allocation for Spain (SDR 9,139 million).<sup>51</sup> The claims on the IMF (€6,588 million), which include the reserve tranche and loans, plus the new allocation (€10,977 million).<sup>52</sup>  $(6,588+10,977) / (67,105+10,977)$ .

## 3.2 SDR operations

As Chart 2 shows, the total amount of SDR holdings is lower than the drawing rights allocated. This is consistent with the sign of the most common operations in a country such as Spain and generates a direct cost for the difference between the interest received and the allocation charges paid. There are, however, two other asset items – loans and the reserve tranche – which also accrue interest and generate income for the Banco de España.

Overall, the most common transaction in the case of Spain is for the Fund to ask the Banco de España to sell SDRs to third countries that need them to pay interest and repay principal on IMF loans. The opposite, i.e. when the IMF asks the Banco de España to purchase SDRs from third countries in exchange for euro that they need for their ordinary financial market transactions, has been less frequent. SDRs have also been provided under loan agreements in the case of SDR-denominated loans (see the following details of the operations performed and the actual or potential use of the SDR holdings).

### 3.2.1 Quota increases

In 2016, the Banco de España paid its quota subscription in euro.<sup>53</sup> The IMF expressed a preference for payment in euro rather than in SDRs.

### 3.2.2 Borrowing arrangements

Regarding the existing Standing Borrowing Arrangements, the resources under the New Arrangements to Borrow (NAB)<sup>54</sup> and Bilateral Borrowing Agreements (BBAs)<sup>55</sup> are available exclusively in euro. In the case of the PRGT (see Box 3) there are two agreements in force. The 2009 agreement<sup>56</sup> (resources available in SDRs) has been fully drawn since April 2020. The February 2017 agreement<sup>57</sup> has a maximum amount of SDR 1.2 billion available in euro and, therefore, will not affect the SDR holdings.

### 3.2.3 Voluntary trading arrangements (VTAs)

The current VTA, signed in 2009, only envisages euro-denominated operations. A further condition of the VTA is that Spain has indicated that it wishes to maintain a range of between 65% and 135% of the amounts allocated. The IMF endeavours to distribute the burden of operations between countries according to these target ranges. The Fund has made 46 requests to implement the VTA, essentially asking the Banco de España to provide SDRs, and has asked it to purchase SDRs on just three occasions.

<sup>53</sup> In the 2016 issue, half of the countries opted to pay their quota subscription in SDRs (see a note in Box 4 on the changes in the IMF's SDR holdings). Under Article 1 of Law 13/1999, the IMF may determine which currency – SDR or other – is to be used.

<sup>54</sup> The New Arrangements to Borrow (NAB) are the IMF's second line of defence, after the quotas, to supplement its resources in the event of difficulties in the international monetary system. Through the NAB, a group of countries stand ready to lend additional resources to the IMF.

<sup>55</sup> The third line of defence, after the quotas and the NAB, as indicated in the previous footnote.

<sup>56</sup> The 2009 agreement was extended in 2014 and is available to the Fund up to 31/12/2024.

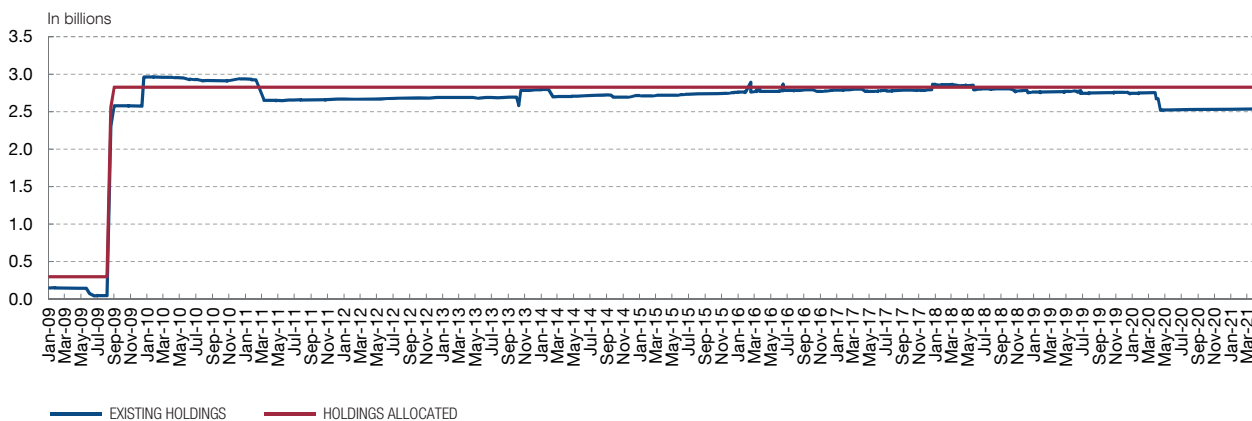
<sup>57</sup> The February 2017 agreement was extended in January 2020 and is available to the IMF up to 31/12/2029.

Chart 2

### SPAIN'S SDR HOLDINGS

Over the period shown Spain's SDR holdings are mostly below the allocations received, reflecting a negative net SDR position.

SPAIN: SDRs ALLOCATED



SOURCE: Banco de España.

### 3.3 Potential change to voluntary trading arrangements (VTAs)

As indicated earlier, given the size of the latest SDR allocation and the needs to be met, especially by some countries, it is reasonable to assume that the IMF is updating its operational procedures to enhance the mobilisation of SDR holdings.

First, given that many euro area countries' agreements envisage the euro as the only currency for which SDRs may be exchanged – to strengthen the international role of the euro – one possible change to be considered could be to use other currencies for these transactions. From an operational standpoint, in accordance with each country's individual reserve management policy, it would be feasible to accept requests for the purchase or sale of SDRs against US dollars (and other currencies) as follows:

- Purchase of SDRs:
  - Against US dollars held in the portfolio of the national central bank responsible for the exchange agreement. The central bank would record entry of SDRs against delivery of US dollars. This would entail a change in the composition of reserves (more SDRs and fewer US dollars), but no increase in the euro money supply.
  - By obtaining US dollars (in exchange for euro) on the markets. This could result in profit or loss, according to the exchange rate applicable, and entails an injection of liquidity in euro.

- Sale of SDRs: in exchange for US dollars which, assuming there is no desire to increase the US dollar position, would be sold on the market in exchange for euro. This entails a liquidity drain.

Furthermore, as discussed above when setting out the options for mobilising SDR holdings, given the volume of SDRs allocated following the expansion, it would seem advisable to expand the group of market-makers for SDRs under the voluntary arrangements, to ease the present situation where these operations are concentrated on the group of 32 countries that currently cooperate under the VTAs. This would also help rebalance SDR holdings.

## 4 Conclusions

The proposed new SDR allocation, which triples the previous stock of SDRs, must be analysed together with the mechanisms for mobilisation of the SDRs to contribute liquidity, in their capacity as a reserve asset, to the countries facing most difficulties during the pandemic. For this reason, it is key to provide a description of the allocations, to put their size in context and to analyse how the IMF manages the transactions required to mobilise the SDRs.

In this respect, the key proposal consists in monitoring the ratio of the net SDR position in the IMF's SDR Department's financial statements to the total amount of SDRs allocated, as a measure of their effective liquidity. This ratio is based on the fact that SDR issuance can only be considered effective once the SDRs have been mobilised via the authorised transactions, as the allocation per se is simply a formal proposal for their generation.

Given the volume of SDRs following the new allocation, and bearing in mind both the 2009 experience and the fact that they are allocated in accordance with the quotas, it could be appropriate to review some of the institutional arrangements that form the framework for SDR transactions. In particular, the number of countries ready to make the allocations liquid under the voluntary arrangements must be increased, and new mechanisms are needed to make these new resources more readily available in a more efficient manner in view of the objectives sought. According to the IMF, more funds have been contributed to support programmes for low-income countries as a result of this allocation, and a new Resilience and Sustainability Trust is being considered.

Furthermore, against the backdrop of the pandemic-induced crisis, an intense debate arose on the sufficiency of the amount to be approved. According to the Fund, the issuance covers between 30% and 60% of new global reserve requirements, in line with the 2009 allocation. Enhanced transparency and accountability in the reporting and the use of SDRs – terms which arose in the debates prior to the proposal of the new allocation<sup>58</sup> – may also be required. In this respect, going forward the Fund intends to distinguish between two categories of changes in SDR holdings, i.e. whether they derive from IMF operations or SDR transactions. It also intends to publish the Annual Update on SDR Trading Operations and, in addition, in two years' time, IMF staff will prepare a follow-up report on the SDR transactions and their macroeconomic impact.

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<sup>58</sup> In particular, the US Secretary of the Treasury indicated the need for enhanced transparency and accountability.

**SPECIAL DRAWING RIGHTS****Not a currency**

SDRs were created in 1969 to supplement international foreign reserves.<sup>1,2</sup> They are neither a currency<sup>3</sup> nor a claim on the IMF.<sup>4</sup> In operational terms they are a potential claim on the freely usable currencies<sup>5</sup> of the countries that are members of the SDR Department.<sup>6</sup> SDRs are formally classified under foreign reserves and are reflected as such on the balance sheet of member countries' monetary authorities.

SDRs consist of a cooperative arrangement between the members of the IMF's SDR Department, whereby an initial entry is made for the allocation, which can be converted pursuant to certain rules. Participants undertake to collaborate with the IMF and among themselves to facilitate the proper use of SDRs and the effective functioning of the SDR Department. The status of SDRs derives from the commitments of members to hold and exchange them and to accept their value as determined by the IMF.

As such, SDRs are a source of liquidity for any country that decides to use them, and only when they are used do they effectively become a reserve asset. The SDR regulatory framework is set out in the corresponding sections of the Articles of Agreement, which include as one of their objectives making the SDR the principal reserve asset in the international monetary system.<sup>7</sup> The SDRs supplement other operations for obtaining currency under different IMF programmes.<sup>8</sup>

SDRs may only be held by member countries. However, as an exception, balances in SDRs may also be held by the IMF itself

(specifically by the GRA Department) and by some international and monetary organisations (known as "prescribed holders").<sup>9</sup> Prescribed holders do not receive allocations<sup>10</sup> and their operations are more limited as they do not participate in the SDR Department. Lastly, SDRs cannot be held by private entities or individuals.

An SDR allocation does not entail direct costs. Assets and liabilities stemming from the allocation accrue the same rate of interest.<sup>11</sup> Consequently, only when there is a difference in the assets derived from the allocation (there are no changes on the liabilities side) do interest receipts or expenses arise for creditor and debtor countries, respectively. This means that if a country's SDR holdings are below its allocation, charges must be paid to the IMF in net terms. Conversely, if a member country's SDR holdings exceed its allocation, it becomes a net recipient of interest. As the net holders receive the interest paid by members that have used their holdings, the SDR Department receives no net income. The return obtained by the creditor countries would be associated with the seigniorage<sup>12</sup> of the issuer. In the case of the Eurosystem, the seigniorage revenue would be shared among the Eurosystem members.

**Determining the SDR value and interest rate**

There is no market that tailors supply and demand via exchange or interest rates. It is the IMF that ensures the system's liquidity. The SDR value is calculated in terms of the US dollar,<sup>13</sup> based on the exchange rates observed daily at 12:00 London time of the SDR basket currencies, as the sum of the US dollar market

1 SDRs were created in 1969 under the First Amendment of the 1944 Articles of Agreement of the IMF.

2 Paul Samuelson called them "paper gold", in comparison with "metallic gold" as a primary reserve.

3 Nevertheless, some texts state that they are a currency, as a currency has three functions: as a unit of account, a store of value and a medium of exchange. SDRs meet these three criteria but are used exclusively by governments and some international organisations. There is a debate about the potential uses of SDRs in these three roles, which goes beyond the aim of this paper.

4 They are therefore not a liability of the IMF.

5 The US dollar, euro, Japanese yen, pound sterling and Chinese renminbi. In practice, the freely usable currencies are the US dollar and the euro. The inclusion of the euro is unique as it is a currency of a monetary union that is not issued by one single member country. The weight of these currencies in the SDR is set every five years to determine the amounts (number of units) of each currency in the SDR basket. The currency amounts are currently: 0.58252 for the US dollar, 0.38671 for the euro, 1.0174 for the Chinese renminbi, 11.900 for the Japanese yen and 0.085946 for pound sterling.

6 It is useful to consider the SDRs as being under an international treaty. Also, given the possibility of adopting an agreement on their cancellation, it should be borne in mind that obligations and rights would arise for debtor or creditor countries or institutions.

7 Article XXII of the Articles of Agreement.

8 Such as the Stand-By Arrangements, the programmes geared especially towards low-income countries (e.g. the PRGT), and short-term transactions (purchases).

9 There are 15 prescribed holders: four central banks (European Central Bank, Bank of Central African States, Central Bank of West African States and Eastern Caribbean Central Bank); three monetary institutions (Bank for International Settlements, Latin American Reserve Fund and Arab Monetary Fund); and eight development banks (African Development Bank, African Development Fund, Asian Development Bank, International Bank for Reconstruction and Development and International Development Association (both of which are World Bank Group institutions), Islamic Development Bank, Nordic Investment Bank and International Fund for Agricultural Development).

10 Nor are allocations made to the IMF.

11 The interest rate as at April 2021 was 0.05%. Under IMF rules this is the minimum rate or floor, i.e. a lower or negative rate will not be applied. The IMF distinguishes between the interest received by members on holdings and the charges they pay for allocations. The rate is the same in both cases.

12 The concept of seigniorage is usually limited to the revenue obtained from banknote issuance by central banks. Here it is used in a broader sense to refer to the revenue obtained from issuing currency.

13 The SDR value was initially defined as the value of 0.888671 grams of gold, which at that time was equivalent to one US dollar. After the collapse of the Bretton Woods system of fixed exchange rates, it was redefined as a basket of currencies.



Box 1

### **SPECIAL DRAWING RIGHTS (cont'd)**

values of the five basket currencies. The interest rate is determined weekly, based on the money market rates of the aforementioned SDR currency basket. The basket currencies and their weights are

reviewed periodically to ensure they reflect their relative importance in trade and capital flows (the renminbi was added to the basket in October 2016).<sup>14</sup>

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**14** The next review will be carried out in mid-2022 and become effective on 1 August 2022.

## ALLOCATION CHARACTERISTICS

## What does allocation entail?

For a member country, allocation technically entails an accounting entry on the assets side of its central bank's balance sheet for the increase in reserves and another entry on the liabilities side for the SDRs allocated. Recording entries on both sides of the balance sheet increases its size in the amount of the allocation, as such balances must be presented gross, rather than on a net basis. The asset entry requires no further explanation: *it represents the receipt of new assets*. An entry is also made on the liabilities side, as the allocation is formally subject to repayment or cancellation and it accrues interest payable.<sup>1</sup> Following the allocation, the amount of "Special drawing rights allocated" on the liabilities side will remain unchanged.

All SDR operations are intermediated by the IMF's SDR Department.<sup>2</sup> This department keeps a "ledger" of transactions and operations involving SDR holdings<sup>3</sup> (see Table 1) and acts as a match-maker for transactions between participants, both through the arrangement of voluntary exchanges (including two-way transactions between members) and with other international institutions.

Initially, as each member country's holdings are equal to the rights allocated, no balances are presented in the SDR Department's ledger. When SDRs are bought or sold, a country's holdings may

fall below its allocations, in which case the difference is recorded under assets (and that country is shown as a debtor), or they may rise above its allocations, in which case the difference is presented under liabilities (and the country is shown as a creditor). In this example, the country purchasing the SDRs will now have an SDR debit balance on its balance sheet and its assets will be higher than its liabilities; conversely, the country selling the SDRs will have an SDR credit balance on its balance sheet.

SDRs can be understood as not having been issued until they are used, i.e. when the net balance<sup>4</sup> of SDR holdings on central banks' balance sheets ceases to be zero. Since these two balances of different sign are held with different entities (one as creditor and the other as debtor), SDRs are issued and may be classed as a financial instrument.<sup>5</sup> As explained in Section 2 of the body of the text, the liquidity of SDRs is evidenced through their reflection in the SDR Department's balance sheet. The example involving two countries needs to be extended to the 190 member countries of the IMF. The balances will be presented in the corresponding financial statements of the IMF's SDR Department, in addition to in each country's balance sheet.

A simulation for two countries (Spain and Benin) is provided below (see Tables 2 and 3). The new SDR allocation is included, in proportion to the respective quotas, in the related balance sheet

Table 1  
BALANCE SHEET OF THE IMF'S SDR DEPARTMENT (a)

SDR million

| ASSETS                                       |               | LIABILITIES                                  |               |
|--|---------------|--|---------------|
| Net charges receivable                       |               | Net interest payable                         |               |
|  | 5             |  | 5             |
| Participants with holdings below allocations |               | Participants with holdings above allocations |               |
| Allocations                                  | 111,895       | SDR holdings                                 | 100,117       |
| SDR holdings                                 | -80,405       | SDR allocations                              | -92,302       |
| Allocations in excess of holdings            | 31,490        | Holdings in excess of allocations            | 7,815         |
| <b>Total assets</b>                          | <b>31,495</b> | Holdings, GRA Department                     | 22,203        |
|  |               | Holdings, prescribed holders                 | 1,472         |
|  |               | <b>Total liabilities</b>                     | <b>31,495</b> |

SOURCE: Banco de España.

a At 30 April 2021.

1 Pursuant to the sixth edition of the IMF's Balance of Payments and International Investment Position Manual.

2 This department was established by the IMF to manage and record all SDR-related matters.

3 Countries must participate in the SDR Department in order to receive allocations. All IMF members are currently members of this department.

4 The difference between the assets and liabilities sides for SDRs, i.e. SDR holdings vs allocated SDR.

5 International accounting standards define a financial instrument as a contract that gives rise to a financial asset of one agent and simultaneously a financial liability or equity instrument of another agent.

Box 2

**ALLOCATION CHARACTERISTICS (cont'd)**

entries. A subsequent transaction, whereby Spain purchases SDRs from Benin in exchange for euro, is reflected. Following this transaction, Spain's balance sheet will record an asset for the SDRs purchased, and the sale of euro, whereas for Benin, the

SDRs on the assets side of its balance sheet will be replaced by euro. On the SDR Department's balance sheet, Benin and Spain will appear as a debtor and creditor, respectively, in terms of SDR holdings.

Table 2  
CHANGES IN BALANCE OF HOLDINGS FOR TWO COUNTRIES OWING TO SDR TRANSACTIONS

Example based on the data of the 2021 allocation for Spain and the Republic of Benin.

| In millions | Spain's SDR balance |                 | Benin's SDR balance |                 |
|-------------|---------------------|-----------------|---------------------|-----------------|
|             | Assets (a)          | Liabilities (b) | Assets (a)          | Liabilities (b) |
|             | 9,139               | 9,139           | 119                 | 119             |
|             | 119                 |                 | -119                |                 |
| Balance     | 9,258               |                 | 0                   |                 |

|  | Spain's € balance |             | Benin's € balance |             |
|--|-------------------|-------------|-------------------|-------------|
|  | Assets            | Liabilities | Assets            | Liabilities |
|  |                   | 150         | 150               |             |

SOURCE: IMF.

- a Balance of holdings.
- b SDRs allocated.

Table 3  
BALANCE SHEET OF THE IMF'S SDR DEPARTMENT VIS-À-VIS TWO COUNTRIES

Example of how SDR transactions between two countries are recorded.

| SDR million                                  |            | SDR million                                  |            |
|--|------------|--|------------|
| ASSETS                                       |            | LIABILITIES                                  |            |
| Participants with holdings below allocations |            | Participants with holdings above allocations |            |
| Benin  |            | Spain  |            |
| Allocations                                  | 119        | SDR holdings                                 | 9,258      |
| SDR holdings                                 | 0          | SDR allocations                              | -9,139     |
| Allocations in excess of holdings            | 119        | Holdings in excess of allocations            | 119        |
| <b>Total assets</b>                          | <b>119</b> | Holdings, GRA Department                     | —          |
|  |            | Holdings, prescribed holders                 | —          |
|  |            | <b>Total liabilities</b>                     | <b>119</b> |

SOURCE: IMF.

### THE IMF'S ROLE IN INTERNATIONAL RESERVE MANAGEMENT

International organisations are set up to address specific needs and attain certain goals. In the case of the IMF, it was created at a time of a shortage of reserves that was hampering international trade, with the aims of promoting international trade from a multilateral monetary base and assisting member countries with balance of payments difficulties. As mentioned, the IMF is tasked with providing short-term loans to member countries and facilitating external reserve management. Thus, with 190 members at present,<sup>1</sup> it has a global vocation in the realm of monetary cooperation. Its decisions are addressed to the member countries, which have to approve or authorise measures for their implementation.<sup>2</sup>

The IMF's resources comprise the currencies received from its members through the quota mechanism.<sup>3</sup> Each country pays 25% in hard reserves, freely usable currency or SDRs,<sup>4</sup> and 75% is deposited in local currency at the IMF's disposal. The IMF's effective resources comprise the reserves deposited by members (the aforementioned 25%), plus the local currency portion of the quota (the other 75%), but only in the case of those countries considered to be financially sound.<sup>5</sup> Consequently, the effective lending capacity is equivalent to around one-half of the quotas.

A standard lending operation is described below in simplified terms. For example, let us imagine that Brazil needs to obtain CNY<sup>6</sup> 1 billion. To do this, it purchases the CNY from the IMF by providing an amount in BRL<sup>7</sup> calculated at the exchange rate determined by the IMF. The IMF will provide the CNY to Brazil, either against its reserve holdings (from the reserve tranche of the quotas) or by requesting that the CNY issuer provide the currency against the local currency portion of the quota at the IMF's disposal (thereby involving a third country). In the first case, the composition of Brazil's reserves held by the IMF changes (reduction in the reserve tranche of the quota and increase in the local currency portion), and there is no cost for the borrower as it uses the reserve tranche.<sup>8</sup> In the second case, the country issuing the CNY (the third country in the transaction) will see an increase in the reserve tranche of its quota and, as this

transaction is for operational purposes a loan, the IMF will levy a surcharge<sup>9</sup> on the country borrowing the reserves, based on the amount and repayment period. The repayment will be made when the borrower country (in this case, Brazil) "repurchases" its domestic currency in exchange for SDRs or other currencies. The currency "requested" in the purchase may be any issued by a country that has a sound financial position (the so-called "usable" currencies). In monetary aggregate terms, these currency purchase and repurchase operations affect the monetary base of the currencies involved.

Reference is made above to the IMF's effective lending capacity relative to the quotas, which are its principal source of funds for loans. The quotas may be supplemented by a second and third line of defence, which are, respectively, the New Arrangements to Borrow (NAB) and the Bilateral Borrowing Arrangements (BBA). Through these arrangements, a group of countries and institutions have committed to providing certain amounts of funds that are available for activation by the IMF.

Moreover, given the difficulties faced by heavily-indebted low-income countries in establishing economic programmes that strengthen their balance of payments position on a sustainable basis and foster economic growth, an additional fund was created to provide financial support on advantageous terms<sup>10</sup> to these countries. This lending programme – the Poverty Reduction and Growth Trust (PRGT) – is financed by contribution commitments from a set of institutions. The IMF acts as trustee and draws on the resources available under these commitments.

In sum, the IMF's lending potential derives from the quotas, loans and specific support programmes such as the PRGT. Unlike the quotas and supplementary lending programmes, the SDR allocation does not form part of what is strictly understood as resources for the Fund. However, given their status as reserves, they can be considered part of the global financial safety net<sup>11</sup> which the IMF aspires to coordinate.

<sup>1</sup> The latest member to join the IMF (and the SDR Department) was the Principality of Andorra, in October 2020.

<sup>2</sup> As indicated in footnote 30 in the body of the text, no sovereignty is ceded to the IMF in this field, as it is an organisation for monetary coordination and cooperation. This means that its decisions are not applied directly; instead, their practical implementation is based on the provisions of each country's domestic law.

<sup>3</sup> As regards its funding and purpose, the IMF may be compared with a credit cooperative.

<sup>4</sup> It was initially paid in gold.

<sup>5</sup> The domestic currencies of the financially weakest countries cannot be used as resources.

<sup>6</sup> Chinese renminbi.

<sup>7</sup> Brazilian real.

<sup>8</sup> The cost would be the loss of the remuneration of the reserve tranche.

<sup>9</sup> There is a basic rate – the SDR rate – which is the remuneration of the amount drawn on the reserve tranche received by the country that provides the reserves.

<sup>10</sup> Concessional lending, with advantageous maturities and interest rates (currently 0%).

<sup>11</sup> An anti-crisis mechanism available to governments, consisting of the aggregate of several levels: internally, the currency reserves or fiscal buffer; bilaterally, swap lines; at regional level, Regional Financing Arrangements; and at the global level, the IMF itself.

**DESCRIPTION OF THE EFFECTIVE SDR LIQUIDITY RATIO**

The proposed ratio is based on the fact that SDRs can only be considered to be effectively issued once they have been used following the authorised transactions, as the allocation per se is simply a formal proposal for their generation. Consequently, it is proposed to monitor the net SDR position in the financial statements of the IMF’s SDR Department, taking as a starting point the negative net position. This is the net open SDR position for the set of countries whose holdings are below their allocations, which will be considered in relation to the total amount of SDRs allocated. Once this negative net position and the liquidity ratio have been obtained, data on the positive net position will be presented in order to focus on analysing its components and changes therein. The analysis is based on observed data and is a first approximation, given the lengthy period of time involved and changes in the Fund’s operations.

The data for the Fund’s fiscal year-end show that, following the 2009 allocation (when the SDRs allocated increased from SDR 21.4 billion to SDR 204 billion), and as the SDRs effectively used held at similar levels (around SDR 9 billion), the ratio fell sharply, from an average of 38% in the period to 2009 to an average of 7% in the period to 2016. It has since held steady at an average of 16%. The reason for the drop in the ratio after 2009 stems from the increase in SDRs available after that year’s allocation, compared with the small variations in SDRs used. Nevertheless, the use of SDRs increased considerably in 2016. This was attributable to a quota increase for all member countries (doubling the previous amount) that became effective that year, with some member countries deciding to pay the subscription out of their SDR holdings, for an amount of SDR 21 billion.

So far we have analysed the volume of SDRs issued from the standpoint of the negative net position, i.e. the net open position as a result of the SDRs used by those countries whose SDR holdings are lower than their initial allocation. As the SDR Department’s financial statements at 30 April 2021 show, this negative net position amounted to SDR 31,490 billion. This negative net position has a balancing entry in the form of a positive net position with three types of counterparties: first, those countries with holdings above allocations; second, the IMF; and third, the prescribed holders. In the case of the IMF and the prescribed holders, the positions stem from SDR operations and transactions, as they do not receive allocations. Chart 2 shows changes in the share of each of these three agents in the total positive net SDR position.

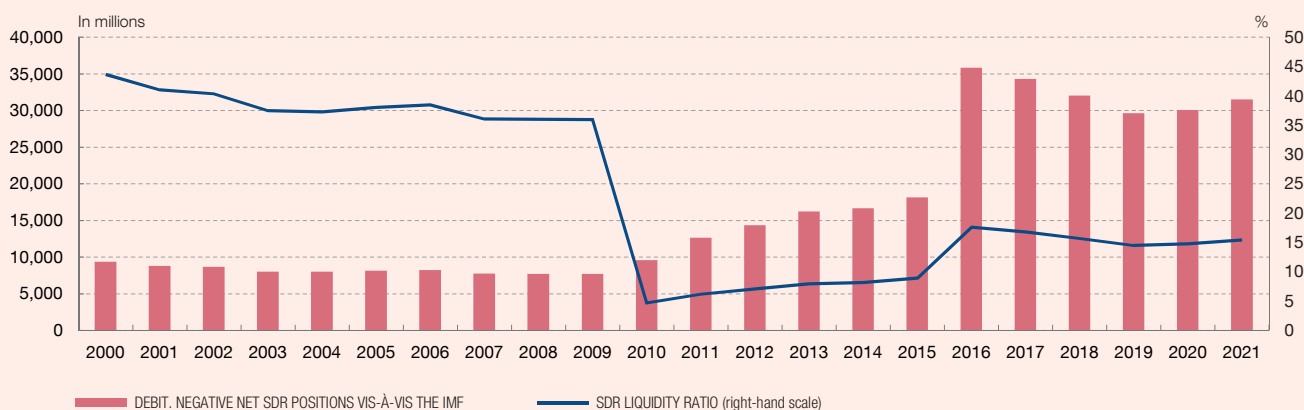
Thus, since the (also very substantial) SDR allocation in 2009, it has been the IMF, via its GRA Department, whose share of the positive net position has increased considerably. This is so in a first approximation, because the more SDRs available, the more likely they are to be used to settle obligations to the IMF. Moreover, owing to the IMF quota increase in 2016, some countries paid the corresponding portion of the quota out of their SDR holdings, in a total of SDR 21 billion. This explains the further increase in the GRA Department’s share of the positive net position.

Given the level of SDRs available following the new allocation in 2021, these indicators are a tool for studying their effectiveness, together with the changes in the programmes and operations that may be made by the Fund and other agents involved.

Chart 1  
CHANGES IN THE NEGATIVE NET POSITION AND LIQUIDITY RATIO

The negative net position refers to the net open SDR position for the set of countries whose holdings are below their allocations. This amount is considered in relation to the total amount of SDRs allocated.

SDRs: NEGATIVE NET POSITION AND RATIO TO TOTAL AVAILABLE



SOURCE: IMF.

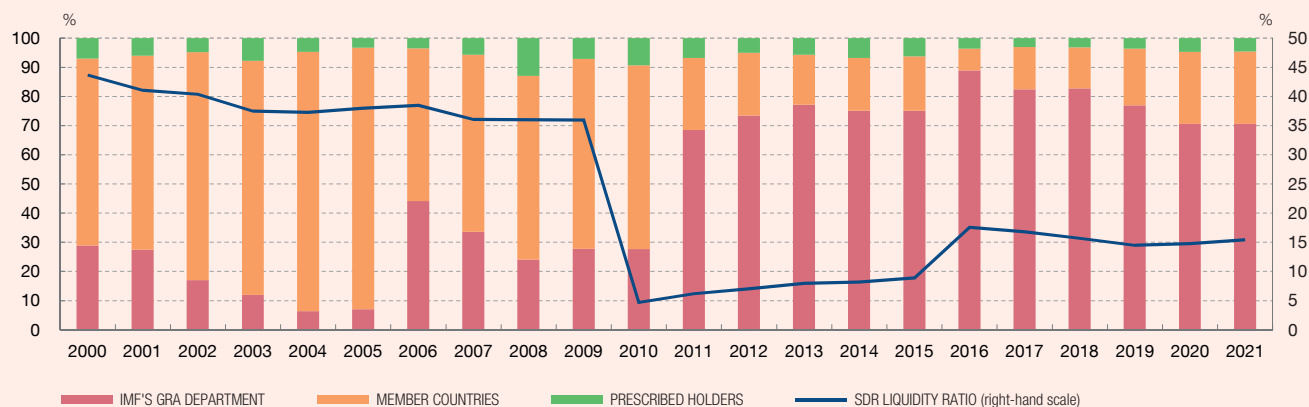
Box 4

**DESCRIPTION OF THE EFFECTIVE SDR LIQUIDITY RATIO (cont'd)**

Chart 2  
CHANGES IN THE POSITIVE NET POSITION AND ITS COMPONENTS

The positive net position is the net open SDR position for the set of countries whose holdings are in excess of their allocations, which is considered in relation to the total amount of SDRs allocated. Changes in the share of each of the three agents in the total positive net SDR position are shown.

SDRs: POSITIVE NET POSITION AND THEIR DISTRIBUTION AMONG AGENTS



SOURCE: IMF.

Table 1  
FINANCIAL STATEMENTS OF THE IMF'S SDR DEPARTMENT

| Amounts in millions                                      | 2008  | 2009  | 2010  | 2011   | 2012   | 2013   | 2014   | 2015   | 2016   | 2017   | 2018   | 2019   | 2020   | 2021   |
|--|-------|-------|-------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Negative net position:                                   |       |       |       |        |        |        |        |        |        |        |        |        |        |        |
| member countries   | 7,707 | 7,704 | 9,556 | 12,633 | 14,341 | 16,197 | 16,622 | 18,138 | 35,832 | 34,278 | 32,007 | 29,596 | 30,055 | 31,490 |
| Positive net position:                                   |       |       |       |        |        |        |        |        |        |        |        |        |        |        |
| member countries   | 4,853 | 5,015 | 6,023 | 3,117  | 3,081  | 2,768  | 3,015  | 3,385  | 2,668  | 4,937  | 4,480  | 5,738  | 7,399  | 7,815  |
| Positive net position:                                   |       |       |       |        |        |        |        |        |        |        |        |        |        |        |
| IMF's GRA Department                                     | 1,852 | 2,133 | 2,635 | 8,644  | 10,522 | 12,494 | 12,462 | 13,617 | 31,842 | 28,256 | 26,472 | 22,772 | 21,204 | 22,203 |
| Positive net position:                                   |       |       |       |        |        |        |        |        |        |        |        |        |        |        |
| prescribed holders                                       | 1,002 | 556   | 898   | 872    | 738    | 935    | 1,145  | 1,136  | 1,322  | 1,085  | 1,055  | 1,086  | 1,452  | 1,472  |
| SDR liquidity ratio                                      | 36%   | 36%   | 5%    | 6%     | 7%     | 8%     | 8%     | 9%     | 18%    | 17%    | 16%    | 14%    | 15%    | 15%    |
| Share of member countries in the positive net position   | 63%   | 65%   | 63%   | 25%    | 21%    | 17%    | 18%    | 19%    | 7%     | 14%    | 14%    | 19%    | 25%    | 25%    |
| Share of the GRA Department in the positive net position | 24%   | 28%   | 28%   | 68%    | 73%    | 77%    | 75%    | 75%    | 89%    | 82%    | 83%    | 77%    | 71%    | 71%    |
| Share of prescribed holders in the positive net position | 13%   | 7%    | 9%    | 7%     | 5%     | 6%     | 7%     | 6%     | 4%     | 3%     | 3%     | 4%     | 5%     | 5%     |

SOURCE: IMF.

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