



From Crisis to Capital: Rethinking the Role of SDRs in Global Development

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Summary

Emerging market developing economies (EMDCs) face escalating challenges in financing development amidst compounding global shocks—pandemics, climate change, geopolitical conflict, and declining aid. In response, the 2021 IMF allocation of Special Drawing Rights (SDRs) offered a vital reserve boost. While the allocation disproportionately favored advanced economies, SDR “recycling” initiatives aimed to redirect resources toward vulnerable countries. The IMF channeled recycled SDRs through traditional lending trusts, preserving their reserve asset status but offering limited fiscal flexibility and scale. A more innovative proposal—using SDRs as hybrid capital in multilateral development banks (MDBs)—could dramatically expand development lending without depleting global reserves. However, central bank resistance and legal barriers have stalled implementation. This paper explores the limits of current SDR governance, the blurry boundary between monetary and fiscal use of reserves, and the potential for reform. It argues that global reserves, though nationally held, are a public good and that modest, risk-mitigated innovations—such as direct SDR allocations to MDBs—could unlock much-needed financing. Ultimately, realizing this potential will require political leadership, collective action, and institutional adaptation at a time of growing economic fragmentation.

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Introduction

Low-income developing countries (LICs) are facing a perfect storm of economic challenges—declining aid, rising debt distress, tighter financial conditions, and escalating geopolitical and climate shocks. While many LICs had a favorable outlook before 2015, lower commodity prices, the slowdown of the Chinese economy, and early signs of debt vulnerabilities began to erode their progress.¹ The COVID-19 pandemic hit LICs especially hard, exposing the limited buffers they had to mount a response. The subsequent Russian invasion of Ukraine disrupted trade and drove up food prices, while rising global interest rates further strained already fragile fiscal positions. In 2025, an expected drop in aid from the U.S. and European donors, coupled with trade uncertainty from renewed tariff threats, has only intensified pressure. The result has been a steady erosion of LIC reserves since 2020. Against this backdrop, the IMF’s 2021 allocation of Special Drawing Rights (SDRs) offered a critical but temporary boost. Yet despite global recognition of the need for sustained development finance, proposals to mobilize SDRs more effectively—particularly through multilateral development banks—have faced legal, institutional, and political barriers. This paper explores how these challenges might be overcome to better harness global reserves for long-term development.

While finding consistent data on reserves across LICs is difficult, the indicative numbers in Figure 1 tell an interesting story. LIC reserves rose slightly as a share of GDP between 2015 to 2020, from 7.6 percent to 9.0 percent, before falling as they were drawn down during the pandemic. In August 2021, the IMF allocated new Special Drawing Rights (SDRs) to all its member countries, which gave a “shot in the arm” especially to LICs.² Figure 1 also shows how LIC reserves may have evolved absent SDRs (simply by subtracting out the August 2021 allocation), which would have fallen by nearly 4 percent as a share of GDP in 2021 alone. Instead, they fell only 1.8 percent. It is difficult to estimate the prudent level of reserves for LICs, but it is likely more than they currently hold, given ongoing balance of payments challenges. For LICs in Africa, the IMF estimates that reserves fell from an average of 2.8 months of imports of goods and services in 2011–2019 to 2.0 months in 2024.³

Hoping that recent events are the last crisis to confront LICs for a while seems wishful if not futile. Over the last decade, as the impact of each negative turn of events seemed to be subsiding, any hope of rebuilding economic buffers was quickly dashed by the next blow. Global tensions are increasing. Tariff wars are heating up. There will be fierce global competition for rare earth metals, many of which are mined in LICs.⁴ Open conflicts are increasing, particularly in LICs and in Africa.⁵ There is increasing resistance to migration from LICs to developed countries, a significant source of reserves accumulation through remittances.⁶ Weather forecasts are for more severe events.⁷ Financial market

1. Lagarde, 2018

2. Georgieva, 2021

3. International Monetary Fund, 2025b

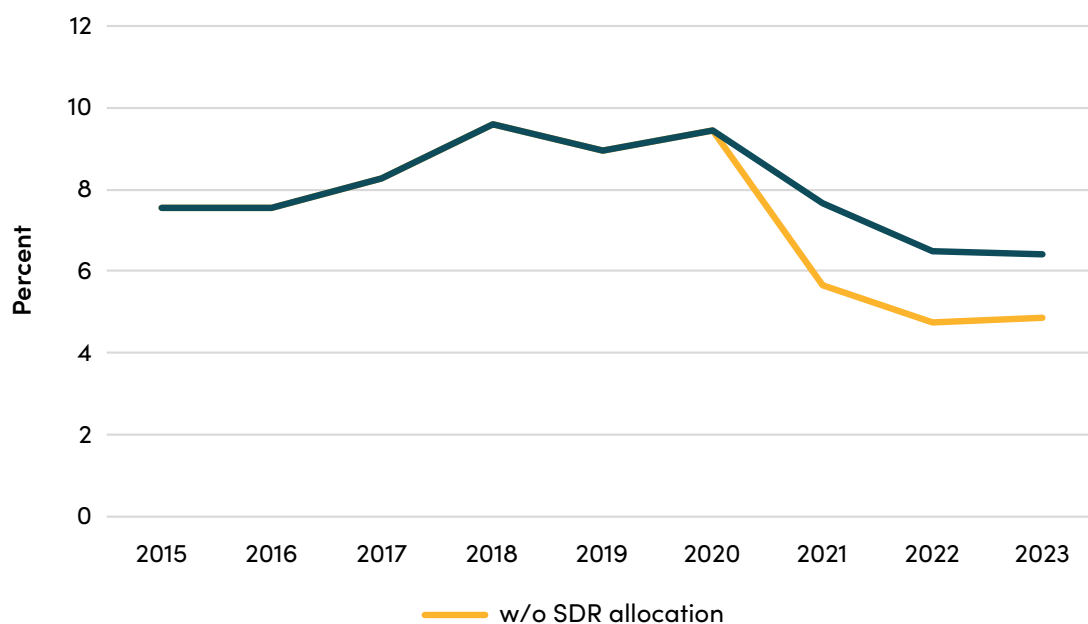
4. Baskaran, 2022

5. World Bank, 2025

6. Henley, 2024

7. World Meteorological Organization, Undated

Figure 1. LIC Reserves to GDP, 2015–2023



Source: (World Bank, 2025)

fragility is more pronounced.⁸ Moreover, those with means are fleeing to gold and other precious metals, and the dollar’s standing as the global reserve currency is being questioned.⁹ Premia on LICs’ bond issuances have increased markedly in the past few years and are not narrowing.¹⁰

Moreover, the financing gap for LICs goes well beyond replenishing reserves. The United Nations’ Sustainable Development Goals (SDGs) provide the global framework for development financing needs. The international community will convene in Seville, Spain, in July 2025 at the Finance for Development Summit to reassess the needs. However, estimates for all developing countries are for about \$4 trillion annually of additional financing.¹¹ While this total comprises domestic and foreign financing, public and private financing, borrowed and unborrowed resources, the number is staggering, growing every year, and likely unattainable by 2030 despite the public rhetoric.¹² Scaling back ambition is an alternative the international community will not yet accept but may be forced to do so by the current global financial climate. The substantive point that can be reasonably extracted from the global hyperbole surrounding the SDGs is that the longer-term financing needs for even more modest development challenges are significant and beyond the scope of developing countries to generate independently. Necessarily, they will demand more public borrowing and increased private sector involvement.

8. Adrian, Malik, & Wu, 2024

9. Pilkington, 2025

10. Landers & Martinez, 2024

11. United Nations Department of Economics and Social Affairs, 2024

12. Organisation for Economic Co-operation and Development, 2025

For LICs to regain a steady development path, they will need to build deeper foreign exchange reserves to serve as buffers for “normal” fluctuations in economic activity; be able to borrow short-term foreign exchange for unforeseen external crises; and have long-term patient external financing to build resilient physical and human capital. The global community’s support for such financing has been haphazard at best. In theory, the International Monetary Fund (IMF) helps countries take the necessary measures to ensure that their reserves are adequate to keep the economy on a steady growth path, providing them with supplemental resources to cover any transitional reserve needs. While very few LICs have access to immediate foreign exchange borrowing provided through central bank swap lines, they can access emergency credit lines from the IMF. Moreover, multilateral development banks, such as the World Bank, the African Development Bank (AfDB), the Inter-American Development Bank (IDB), or some bilateral donors, will provide patient, longer-term development assistance. While much has been written about the adequacy (or rather the inadequacy) of these three pillars of the development finance architecture, there is no doubt that more is needed in each dimension, and there is a paucity of ideas on how to produce more.

The COVID-19 SDR experiment

The world unwittingly experimented with a new form of development finance when the IMF allocated \$650 billion of Special Drawing Rights (SDRs) in August 2021. This emission of reserve assets by the IMF was meant to give a “shot in the arm” to emerging markets and developing economies (EMDEs). Because of IMF allocation rules, high-income countries received nearly 70 percent of the allocation, while upper middle-income countries (including China and India) received over 20 percent. This left almost 9 percent for lower middle-income countries and just over 1 percent, or roughly \$8.5 billion for LICs (Figure 2).¹³ To affect a different allocation of the SDRs would have required a change in the IMF’s Article of Agreement, requiring an 85 percent vote of the membership, which was politically infeasible.¹⁴

The immediate effect was to provide much-needed reserves to LICs’ central bank coffers. However, many LICs quickly “used” the SDRs, converting them to usable currencies, which were spent on various pressing needs.¹⁵ Converting SDRs into usable currencies and then spending them is tantamount to using monetary reserves for fiscal purposes. While each country has regulations regarding what entity makes decisions regarding SDRs (e.g., the central bank or the treasury), these spending decisions were made within each country’s sovereign rules.

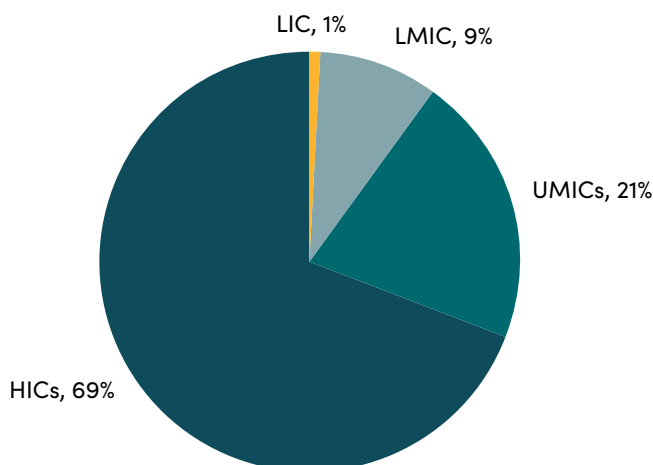
The sovereign decision of some LICs to cross the monetary/fiscal divide—that is to use foreign exchange reserves (SDRs in this case) for non-monetary purposes—was not entirely benign vis-à-vis the foreign reserves of the rest of the world. To “use” the SDRs for fiscal purposes, country

13. Plant & Andrews, What is the Best Way to Allocate New SDRs?, 2021

14. Andrews, How Might an SDR Allocation Be Better Tailored to Support Low-Income Countries?, 2021

15. International Monetary Fund, 2023

Figure 2. August 2021 SDR allocation by income group



Source: International Monetary Fund, 2021

authorities had to exchange their SDRs for the hard currency held by some other country through the IMF's Voluntary Trading Arrangements (VTAs). While these trades are voluntary, they change the composition of the trading partners' foreign reserve assets, skewing them toward SDRs. Holding all other things constant, the LIC will pay interest on the deficiency in its SDR holdings relative to its allocation, and its trading partner will receive an equivalent amount on its now excessive holdings of SDR. Via the SDR mechanism, LICs borrowed some portion of the stock of global hard currency monetary reserves and used them for fiscal purposes.

Advanced economies, which received US\$455 billion of the SDR allocation, did not need them, so the G20 reached an agreement to "recycle" \$100 billion of SDRs to LICs. However, the G20 insisted that any recycling scheme preserve the "reserve asset characteristic" of the SDR. To do so, the most obvious intermediary was the IMF. Well before the pandemic, advanced countries had funded the IMF's Poverty Reduction and Growth Trust (PRGT) with SDR-denominated loans. Funds in the PRGT were lent to LICs under various IMF-supported programs, usually disbursed over three years and repaid over 10 years. The PRGT-based lending from the IMF to an LIC is denominated in SDRs (although it could be disbursed in another currency) and it is ostensibly to comfort the long-term balance of payments position of the LIC. It is generally made from the IMF to the central bank or monetary agency of the LIC, not to the country's fiscal or budgetary authority. This lending model preserves the SDR's reserve asset characteristic as it comforted the LIC's foreign reserves position. If the LIC decides to use the added monetary reserves for fiscal purposes, that is its sovereign decision, and any use of the SDRs does not abrogate the country's obligation to repay its PRGT loan in SDRs. However, like the direct use of their SDRs described above, the country that was spending borrowed SDRs was implicitly crossing the global monetary-fiscal divide by borrowing against the

world's foreign reserves through its conversion of SDRs to hard currency. This is tolerable to central banks because the IMF, a monetary institution, intermediates the loans. The PRGT would absorb any loss from unpaid loans on the PRGT's books and arrange for SDRs to be refunded to the recycling advanced country if needed. In addition to covering these credit risks, PRGT borrowing is structured with adequate buffers to allow lenders to withdraw their SDRs at any time if needed, thereby also preserving the liquidity of these reserve assets.

Concurrently with the discussion on SDR recycling, the IMF was increasingly cognizant of the longer-term needs of EMDEs to confront the impacts of climate change and invest in pandemic preparedness. The SDR allocation opened a financing opportunity to help them. The IMF established the Resilience and Sustainability Trust (RST), funded through recycled SDRs, to give long-term loans to EMDEs to support the adjustments the country had to make to ensure longer-term sustainability. Loans from the RST were made available to more countries than those made through the PRGT, were smaller, had a longer maturity (20 years vs 10 years) and a longer grace period (10 years vs. 5 years).¹⁶ Given this longer time horizon, it stretches credulity to think that the SDRs lent under the RST are for comforting monetary reserves while balance of payments adjustments occur. The fact that they are to be used for fiscal purposes is evident in examining the conditions attached to the loan.¹⁷ Even more than with the PRGT, the acceptance that the reserve money characteristic of the SDR is being preserved under the RST is based on the loans to EMDEs being through the IMF, with institutional safeguards that cover credit risks and assure the SDR-recycling country can access its SDRs on demand should it have a balance of payments crisis.

The expansion of IMF lending to LICs through SDR recycling was seen as a mixed bag by many in the development finance community. While this arrangement protected advanced country interests in preserving the reserve asset nature of their recycled SDRs, it did not provide the volume and type of assistance EMDEs needed to recover from the pandemic and face the balance of payments and fiscal pressure that climate change would bring about. The two trusts at the IMF could not absorb the entire \$100 billion of SDR recycling that the G20 had committed to, and the IMF's reputation was as a recalcitrant lender unresponsive to developing countries' needs. The commitment and disbursement rates were slow and conditional.¹⁸

Three lessons could be drawn from the COVID-19 SDR experiment:

- The COVID-19 financial crisis was fiscal, and throughout the world, monetary tools were used to augment government budgets. The SDR allocation allowed EMDEs to access global monetary reserves to expand their fiscal firepower.
- The inflexibility in the rules governing SDR allocations limits their usefulness in responding to a non-monetary global crisis, and no good reallocation mechanism exists.

16. For details on the RST, see International Monetary Fund, 2024

17. Gupta, 2023

18. Wainer & Plant, 2022

- It is an illusion that SDRs aren't used for fiscal purposes—they were used before, during and after the COVID-19 crisis to help governments adjust their budgets. Global reserves are being lent to help EDMs develop, but through a complex and untransparent system that restrains their effectiveness.

From COVID-19 to climate: the MDB (non) experiment

When the SDR allocation was made, there were many other proposals to use SDRs, but few faced up to the reserve asset nature of the SDR. The large amount of SDRs sitting unused on central bank balance sheets, even beyond those pledged to be recycled, was a tempting source of “manna from heaven” for many worthy causes, including pandemic relief, climate adaptation, agricultural development, etc. The problem with most proposals was that SDRs could not be spent on anything concrete (say, vaccines, seawalls, or seeds). They would first have to be exchanged for hard currencies, which meant tapping some central bank's foreign exchange reserves. Central banks would fiercely resist any such scheme. In what advanced country would the central bank let its reserves be spent on solar panels in a developing country in Africa? What guarantee would there be that their reserves would ever be repaid? Moreover, even if an international crossing of the monetary-fiscal divide were countenanced, why use the clumsy intermediary SDR asset? Why not just raid the coffers of global foreign exchange reserves directly?

The African Development Bank (AfDB) and the Inter-American Development Bank (IDB) made the most tenable proposal for SDR recycling outside the IMF. The institutional underpinnings of the AfDB and IDB made them attractive institutions for a recycling proposal. First, their shareholders were global, including many of the G20 countries that had promised SDR recycling. Second, they have a well-established financial reputation, AAA credit ratings and are governed transparently by their boards. Third, and perhaps most critically, they are designated holders of SDRs. They have SDR accounts at the IMF and can accept and disburse SDRs on their account with member countries and other holders of SDRs. In sum, they are internationally governed institutions that, while not central banks, are already part of the SDR system.

The AfDB and IDB proposed that recycled SDRs constitute hybrid capital in each bank, which would then be leveraged to increase their lending capacity. Advanced countries would lend SDRs to one (or two) of the banks, with provisions that the loans could serve as capital and be liquidated in case of a dire balance of payment needs.¹⁹ The loans were to be remunerated slightly above the SDR interest rate, thus making a small profit for the recycling country. The loaned SDRs would be held in the AfDB and IDB accounts at the IMF and would not be exchanged for hard currency or spent – no central bank would have its hard currency reserves tapped. The ratings agencies agreed that this

19. A 20 percent liquidity reserve should be set aside to ensure liquidation. This is parallel to the financial structure of the IMF's RST and PRGT.

arrangement satisfied the definition of capital, and thus, the banks could leverage the SDR holdings and raise money in global financial markets. Given their leverage ratios, the two banks could then lend to their developing-country clients between 2 and 4 times the amount of SDRs that advanced countries had recycled into their hybrid capital fund. After lengthy consultations, the IMF essentially agreed that this arrangement preserved the reserve asset characteristic of the SDR.²⁰

Besides being institutionally well-grounded, the AfDB and IDB proposal has five advantages:

- Every SDR100 million recycled to the AfDB will be multiplied to increase loans to vulnerable African countries by SDR200–400 million.
- The SDRs are never spent – they are held in an account at the IMF.
- There will not be any calls on central banks' currency reserves through this kind of recycling.
- The hybrid capital model preserves the SDRs' reserve asset characteristic.
- Countries recycling SDRs to the AfDB could make a small profit on their investment.

Despite being publicly discussed for over two years, the hybrid capital proposal has not yet been actualized. Some advanced countries have indicated interest in recycling SDRs to the AfDB and IDB, but none have done so. To make the proposal technically viable, five countries must participate, preferably in equal amounts. With this critical mass of participation, the liquidity of claims could be assured, using procedures that mirror the so-called 'encashment' arrangements in place for the PRGT and RST. Each participant would undertake to allow their SDRs to be drawn upon to meet withdrawals of other participants in the event that they faced an acute need for reserves. However, getting five central banks to agree has become difficult. Strong global leadership from one or two advanced countries is needed to move the proposal, but none has stepped forward. One of the major obstacles has been that countries in the eurozone are prohibited by law from recycling SDRs to any entity other than the IMF. The President of the European Central Bank stated clearly that "the direct financing of multilateral development banks by national central banks of EU Member States through SDR channeling is not compatible with the monetary financing prohibition." Informal proposals to see if the law could be changed met with resistance at the European Central Bank (ECB) and among the various country central banks that govern the ECB. In other countries, ministries of finance and development have often supported such recycling, only to meet opposition from central banks that have a say in managing SDRs.

The opposition to the hybrid capital scheme is grounded in a doctrinal belief that reserve assets should not be used for fiscal purposes, even though the hybrid capital SDRs would not be spent or exchanged for foreign exchange. While no central bank has publicly or formally opposed the hybrid capital scheme, private conversations have indicated a hesitancy to use SDRs in a manner that puts them at risk. But the risks are slim. The only instance in which the SDRs would have to be liquidated

20. The IMF believes it is up to each central bank to determine what it views as a reserve asset. Thus, it was not able to formally deem SDR-based hybrid capital as a reserve asset. However, it did say that if a central bank declared it so, the IMF would count it as a reserve asset in its statistics on central banks' financial situation. See International Monetary Fund, 2024.

would be a capital deficiency at AfDB or IDB so deep that the bank(s) would have to call on the hybrid capital to cover liabilities. Given the conservative management of the banks, the chances of such a capital call are miniscule, if not non-existent. In analyzing the scheme, an independent group deemed the proposed hybrid capital scheme less risky than the RST at the IMF.²¹ When pressed on the lack of logic in their reticence, central bankers retreated to the “slippery slope” argument—that such a scheme, while perhaps safe for the AfDB and IDB, would open the door to other institutions that were less financially solid to use similar schemes that could not be resisted if the AfDB and IDB schemes were indulged.

Moreover, a justified parochialism complements the doctrinal hesitancy—“why should my country’s reserves be put at risk (however minimal)? Let others do it.” Reserves are considered national assets that help protect the country’s macroeconomic stability. In an increasingly turbulent global economic system, with global financial cooperation on the wane and countries cutting (fiscal) aid budgets, why should central banks be taking up the mantle of development assistance? That is a government function, not a central bank function. Central banks resist using reserves to resolve their own country’s fiscal problems. Why should their reserves be encumbered for another country’s challenges?

While each country reasonably protects its reserves, there are sufficient global reserves to support the AfDB and IDB without endangering global financial stability. Global reserve assets stand at about \$12.36 trillion, having receded from their peak value of \$12.93 trillion in 2021. The initial hybrid capital request from the AfDB was for SDR2.5 billion, or about US\$3.5 billion. This is about 0.028 percent of global reserves. Using a conservative leverage rate of 3, this could increase AfDB’s potential loan book from US\$22 billion (as of end-2023) by US\$10.5 billion to US\$32.5 billion—a 50 percent increase in loans to developing countries.²² The IDB has almost twice the loans outstanding of the AfDB, so a similar-sized hybrid capital would be less consequential for the institution but would allow more US\$10.5 billion in lending in the Americas.²³ If a financial catastrophe occurred and all the hybrid capital had to be called and the recycled SDRs had to be liquidated, global reserves would fall by 0.050 percent. This could be consequential for an individual country that had recycled its SDRs into hybrid capital, but at a systemic level, the consequences would be minor and only realized with a very small probability. However, the benefits to developing countries from putting the SDRs at risk as hybrid capital could be great.²⁴

21. Risk Control, 2024

22. African Development Bank, 2024

23. Interamerican Development Bank, 2024

24. Detractors of the MDB model might disagree that expanding the IDB and AfDB’s lending power would be hugely beneficial to developing countries. However, that argument is separate from how they might be funded.

How best to use SDRs for development

The inability of the AfDB-IDB SDR experiment to be brought to fruition indicates a public goods problem that needs to be solved. There is considerable developmental benefit to using some portion of global reserves to augment MDB capital. However, because global reserves are held piecemeal by 200 countries, no individual country is willing to bear the risk of doing so. This unwillingness to take on this risk is compounded by the widespread practice of having central banks be independent from governments. While political leaders are often called upon to sacrifice a country's self-interest for the global public good, they cannot override their central bank's prerogative to manage reserves. Leaders might use moral or political persuasion in a domestic context to move central bank decisions, but to do so across borders would be hard sell.

In essence, the IMF was invented to solve similar public goods problems. IMF member countries contribute capital (quota resources) to the institution to assist countries in confronting acute balance of payments difficulties. The IMF lends to the troubled country to give it the financial space to take necessary economic policy measures; without the IMF loan to provide reserves, economic activity would halt. Going one step further, in 1969, the IMF began to provide countries with SDRs, which can be exchanged for another country's hard currency reserves on demand. Thus, each country has a "right" to borrow global hard currency reserves up to the amount of its allocation of SDRs. Moreover, by recycling SDRs through the IMF's PRGT and RST, eligible LICs and EMDEs can access SDRs beyond their allocation and use them in the context of an IMF program to support medium-term balance of payments problems.

The SDR effectively acts as a foreign reserves credit line, which can provide the buffer needed in EMDE reserves to confront increased volatility in global financial markets. The SDR has no intrinsic value but can be used to purchase hard currency, with the price being the SDR interest rate. The EMDE can receive SDRs by direct unconditional allocation. But this is a blunt tool. Under current rules, an additional allocation can only be made with the approval of 85 percent of the IMF votes (which gives the United States a veto as it has almost 17 percent of the votes) and must be given proportionally to all IMF members, the proportion being determined by quota shares (thus the USA gets 17 percent of any allocation). Alternatively, the EDME can receive additional SDRs through a conditional loan from the IMF, either from the IMF's main balance sheet (the General Resources Account) or from the PRGT or RST. Whether these loans are effective tools for increasing EDME's buffers is a matter of considerable debate and beyond the scope of this paper.

The SDR could also have a role in mobilizing the long-term patient external financing that EMDEs need to build resilient physical and human capital to promote development. The IMF has neither the expertise nor the mandate to finance the longer-term investment needed for steady development progress. Among international institutions, this task is rightly undertaken by multilateral development banks, such as the AfDB, the IDB, and others. The capital of these banks is contributed by countries, both advanced economies and EMDEs, in the form of direct monetary contributions

from country budgets. They have begun to use hybrid capital, which includes private sector money.²⁵ The proposal to use SDRs as hybrid capital is financially sound, but as noted above, it has been blocked by central bank hesitancy and the need for collective action.

The current blockages to using SDRs to capitalize MDBs could be overcome by allocating SDRs directly from the IMF to MDBs as hybrid capital, without going through IMF member countries.²⁶ This scheme would implicitly commit a small amount of global reserves, via the SDR, to the capital of MDBs. The MDB or any member country would not spend the SDRs. No central bank would have to commit its resources. In the unlikely event that the SDR hybrid capital were to be liquidated due to a capital call, the burden could be shared by IMF members in proportion to their quotas, thus spreading the liability across the globe in small amounts. In essence, allocating SDRs directly to MDBs allows each country to contribute to strengthening the MDBs' lending power. The MDBs could then leverage the SDRs in capital markets to increase their lending firepower.

Instituting direct allocation of SDRs to MDBs would not be easy. It would require a change in the IMF's Articles of Agreement, which would require an 85 percent vote of the IMF membership, an agreement on what MDBs or financial institutions would be eligible for such a scheme, when and how often such allocations could take place, and how the size of the allocation would be determined. There would have to be strong leadership from one or more advanced countries to build the necessary consensus on all these issues. It would also require IMF management and staff commitment to work through the myriad technical details.

Some alternative proposals

The 2021 SDR allocation demonstrated that it was a blunt instrument to address a balance of payments crisis that affected only a limited group of countries. While all countries faced economic difficulties in the wake of the COVID-19 pandemic, advanced countries had the monetary and fiscal space to react appropriately. The EMDEs lacked that economic flexibility and needed help. No other instrument was available to give widespread balance of payments help quickly and unconditionally. However, most SDRs went to countries that did not need them. Moreover, the fact that every country received SDRs caused political consternation in the United States Congress and elsewhere, as countries subject to international sanctions or engaged in aggressive military action were receiving SDRs.

There have been calls for targeted SDR allocations, say to EDMs or LICs, instead of allocations covering the entire IMF membership. Such a change would also require an Amendment of the Articles of Agreement, which is a high bar to meet. However, the thornier substantive issue is deciding what countries are eligible and whether to define the decision in the Articles. Is the determination made ex ante or tailored to the impact of a crisis? There is no guarantee that the

25. African Development Bank, 2024

26. Plant & Songwe, Allocate SDRs Directly to Multilateral Development Banks, 2024

allocation would respond to the need if the former. If the latter, a determination of eligibility would have to be made at the time of the crisis, which could devolve into nasty political discussions reflecting current global political (not economic) considerations. It also would raise the question of why the IMF could not use its other lending instruments to address that need.

A subsidiary proposal would use an SDR allocation to assist countries in debt distress. This would face the same formidable bureaucratic challenges as any change to the allocation formula. However, it presents two other difficulties. First, if SDRs were given to a country to repay debt or make debt service payments, the country would essentially be given unconditional access to global currency reserves to pay off some of its debt. Usually, the moral hazard problems of debt relief are mitigated by having an IMF program, with requirements to put the financial house in order. Global political problems could also arise when, for example, a LIC converted its debt-related SDR allocation to dollars through an SDR/dollar exchange with the United States, which it then used to pay off Chinese debt. Second, deciding how big the allocation should be to a country or a set of countries for debt relief would be a fraught technical and political exercise, depending on a forward-looking macroeconomic and debt sustainability analysis and an analysis of creditors' willingness to bear some debt relief burden. These tasks are typically done case-by-case in the context of a debt workout, with lending support from the IMF. How would an SDR allocation be tailored to fit this need?

There have been various calls for a regular global SDR allocation. The Fund's articles of agreement allow for an SDR allocation roughly every five years. However, since 1970, there have been four general allocations and the one special allocation when countries in the former Soviet bloc joined the IMF required an amendment to the IMF Articles of Agreement.²⁷ Analysts have differed over how often and how they should be calibrated. But a regular SDR allocation of a predictable size would allow this form of liquidity to keep pace with the growth of global reserves and GDP and would give EMDEs a predictable source of reserve growth over the long term. The regular allocation could be targeted along the lines of the first suggestion in this section, but that might complicate the political process of getting the reform approved.

Any reform of the SDR mechanism will require a wide global consensus. As noted in the paragraphs above most of the suggested changes would require a super-majority (85 percent) of the IMF members' votes. In any global political context, garnering such a majority would require political and technical leadership. But today's politics are particularly fraught. With the United States holding just under 17 percent of the votes, they hold veto power over any such decision. The first Trump administration blocked the post-Covid SDR allocation, and it is unlikely they would support such changes, although some in the US Congress have suggested changing the allocation formula. In today's highly charged global political environment, it is likely that there could be blocking coalitions for proposals by the US especially if they exclude key global economies, such as China.

27. International Monetary Fund, 2025

Conclusion

The fiscal use of monetary reserves is not a new phenomenon. It is usually a sovereign decision within a country when to spend reserves for non-monetary purposes. But the current international financing architecture allows countries access to global reserves through the IMF, either through borrowing or being allocated SDRs. SDRs, lodged at a EMDE central bank, can be exchanged for hard currency reserves, which in turn can be spent by the EDME government. The intermediation of the IMF in this process assures that the reserve asset characteristic of the SDR is maintained. Nonetheless, the chain of transactions eventually results in the pool of global reserves being tapped for fiscal purposes.

The financial needs of EDMs are only growing. They will need to bolster their reserves to respond to an increasingly shock-prone global economy and spend more on development initiatives. SDRs can be used to address these growing financing needs.

The 2021 allocation of SDRs served as a starting point for this discussion. The allocation provided a critical lifeline to EMDEs, whose balance of payments was severely impacted by COVID-19, both through disruptions to exports and imports. In contrast, advanced economies, with ample reserves and greater fiscal flexibility, had little need for additional SDRs. This disparity led to proposals for advanced economies to “recycle” their SDRs to EMDCs, where balance of payments and budgetary support remained crucial.

The International Monetary Fund (IMF) emerged as the logical institution to facilitate this recycling, given its ability to preserve the reserve asset characteristics of SDRs and maintain the monetary-fiscal boundary at the international level. However, proposals from the African Development Bank (AfDB) and the Inter-American Development Bank (IDB) sought to take SDR recycling a step further—using SDRs to bolster their capital bases and, in turn, expand lending by up to six times the amount recycled.

Despite its small size, the proposal has faced strong resistance from central banks and some national treasuries, which viewed it as an inappropriate use of global reserves for fiscal purposes. Furthermore, no advanced country had an incentive to put its reserves at risk, however minimal, for the common good.

Global reserves constitute an underutilized public good, and innovative financial instruments should be designed to preserve national sovereignty over reserves, mitigate risk, and enhance the ability of global financial institutions to provide essential development and balance-of-payments financing. The SDR provides such a mechanism but will require a global consensus on SDR reform, which may be challenging to marshal amid fractured global politics.

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