PRESENT AND FUTURE ROLE OF THE SDR

In April 1996 the Executive Board met to discuss the conclusions of a seminar held in March 1996 on the future of the SDR—the international reserve asset created by the Fund in 1969 to supplement existing reserve assets. The seminar had been organized in response to a request by the Interim Committee at its April 1995 meeting for "a broad review, with the involvement of outside experts, of the role and functions of the SDR in light of changes in the world financial system" (*Annual Report, 1995,* page 210). The seminar was designed to clarify some of the key issues and differences of opinion about the SDR's role in the international monetary system (Box 2).[6]

Directors agreed that the seminar had helped to meet the Interim Committee's mandate for a general review of the SDR and noted that several themes had emerged from the discussions. Directors observed that there was little support for the provision in the Articles of Agreement that the SDR should become the principal reserve asset of the international monetary system. Directors noted that, under the present SDR system, many Fund members had never received SDR allocations or had not participated in all the allocations, and that this gave rise to concerns about equity. There was also support among Directors—but not the very broad majority needed—for periodic general SDR allocations on the basis of the criterion of long-term global need set forth in the current Articles. Views differed about whether the existing wide divergences among member countries in the costs of obtaining reserves made a case either for an SDR allocation under the present Articles or for an amendment of the provisions of the Articles governing allocation.

[6]The papers presented at the seminar will be forthcoming in a seminar volume.

Directors indicated no change in their earlier positions regarding the case for a general SDR allocation. Those who favored an equity allocation—that is, distribution of SDRs to those members that had never received them or had not participated fully in previous allocations—reconfirmed the widespread desire to achieve the objective of full participation of all members in the SDR system, including receipt of SDR allocations. Several Directors insisted, however, that equity-related allocations should be linked to a general allocation, in keeping with the present Articles. Some Directors supported further study of targeted allocations as a possible compromise on the widely diverse views on general allocations.

Some Directors felt that if the Articles relating to the SDR were amended, provisions should be introduced authorizing commercial banks and other private institutions to hold SDRs. A few Directors also supported the idea of encouraging other official institutions to use the SDR more extensively. Although many Directors noted with interest that several proposals relating to SDR valuation and interest rates were put forward by seminar participants, in general Directors did not take the view that the present valuation and interest rate characteristics of the SDR posed any serious problems.

Directors agreed that there should be renewed efforts to resolve the equity issue as soon as possible. They indicated that they remained open to considering some of the proposals raised during the SDR seminar, but only if and when it became apparent that these proposals could attract the necessary broad support or contribute more generally to progress on allocation issues. After considering the Board's report on the seminar on the SDR, the Interim Committee in April 1996 requested the Board to reflect further on proposals on the role of the SDR and to reach a consensus on a way for all members to receive an equitable share of cumulative SDR allocations.

Box 2

SDR SEMINAR ADDRESSES SEVERAL ISSUES

The seminar on the future of the SDR, held in March 1996, brought together a number of outside experts as well as Fund staff. Some of the key questions addressed at the seminar included:

- Does the global economy still benefit from the existence of the SDR?
- Would the SDR's benefits be enhanced by an allocation targeted at specific groups?
- How could the SDR be redesigned to make it more attractive to private financial markets?
- Is the SDR likely to become the principal international reserve asset, an objective set forth in the Articles of Agreement?

Three broad themes emerged from the seminar discussions:

- The prospect of the SDR being established as the principal reserve asset of the international monetary system is unlikely. Nor does the SDR appear destined to evolve from an unconditional line of credit into a full-fledged world currency. Some proposals, requiring amendments to the Articles, were put forward, however, that could facilitate greater demand for SDRs, within the public and private sectors.
- The SDR should not be abolished, because it might provide a valuable "safety net" if the international monetary system got into serious difficulties.
- The Fund and the international community agree on the need to find ways to solve what is known as the equity issue—that is, the fact that many Fund members have never received an SDR allocation.

Other points emerging from the seminar included:

- The impasse over SDR allocations reflects the continuing lack of consensus on how to interpret the criterion for allocation under the Fund's Articles—that there must be a "long-term global need" to supplement existing reserves. On the one hand, several speakers at the seminar emphasized that, although the demand for international reserves is expected to increase in line with the growth of world output and trade, it could be argued that "global need" does not necessarily mean that a large majority of members must simultaneously face a need to supplement their existing reserves. Since the great majority of the Fund's membership faces costs of holding reserves that are substantially higher than the true economic costs of creating reserves, it could be argued that an SDR allocation would meet the criterion of global need. On the other hand, others maintained that the growth in world trade over the past decades does not appear to have been hindered by the limited supply of SDRs, and an expansion of SDRs would not necessarily help to increase world trade. Further, there is currently no shortage of liquidity in the international monetary system, and the current regime of floating exchange rates has nullified the danger of systemic instability in the absence of the creation of additional reserves. Countries could acquire reserves—albeit at a cost—by running a current account surplus or a capital account deficit. The view was also expressed that creating freely usable exchange reserves through SDR allocations for support payments to needy countries would not be appropriate and would be detrimental to the adjustment process.
- Although the present Articles do not permit selective or targeted allocations, some speakers were of the view that a case might be made for a global allocation followed by a voluntary post-allocation redistribution to those countries that would benefit from an enhancement of their reserve assets. Alternatively, amendments to the Articles for a targeted equity allocation could be considered.