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Special Drawing Rights and Development Aid

by Dr Hans-Dieter Hanfland, Bonn

On October 24, 1970, the UN General Assembly adopted the Strategy Document for the Second Development Decade. This document which will be the basis of development policy in the next years contains the demand of the developing countries for a link between the Special Drawing Rights (SDR) and development aid. The document says under No. 52: „As soon as adequate experience is available on the working of the scheme of Special Drawing Rights, serious consideration will be given to the possibility of the establishment of a link between the allocation of new reserve assets under the scheme and the provision of additional development finance for the benefit of all developing countries. The question will, in any case, be examined before the allocation of Special Drawing Rights in 1972.“

The Demand of the Developing Countries

Two possible forms of procedure have been mentioned in the discussion hitherto as regards the implementation of this idea of creating a connection between SDR's and development aid which has become known under the term "link":

☐ Part of the annual SDR allocations destined for industrialised countries is transferred to the International Development Association (IDA). IDA uses them to procure the national currencies of industrialised countries which it requires for its loans to developing countries. This "direct" or "organic" link would presuppose another amendment of the IMF Articles of Agreement as IDA cannot be authorised to acquire or use SDR's under the currently valid regulations.

☐ IDA is not given any SDR's but the industrialised countries put the equivalent of a certain percentage of their SDR allocations at its disposal in convertible currency. This method of establishing an "indirect" link does not require amendment of the IMF Articles of Agreement.

For some time the developing countries have lodged the demand in all international bodies which in their opinion provide a suitable forum that the question of the link should be clarified by 1972 at the latest. They regard this date as advantageous because the decision on further SDR allocations for the second Basic Period

which under the IMF Articles of Agreement will cover five years must be taken in 1972.

Following an intensive discussion centering on the study of a group of experts¹ the LDC's presented a draft resolution for the link to the Finance Committee of the World Conference which was however rejected by the industrialised countries. The constellation was the same at the meeting of the World Trade Council in October 1970. The deep rift separating industrialised and developing countries over this issue also showed at the last annual meeting of the IMF in Copenhagen in September 1970 although the fronts were by no means solid on either side. A large number of LDC's expressed themselves in favour of first examining the possibility of a link in the IMF. Few of them went beyond the demand for a study of the subject and took already a clear stand in favour of the link. Many LDC's showed a remarkable reserve in their statements on the problem.

Arguments in Favour of the Link

The idea of a link was broached already in the initial schemes for a rational supply of international liquidity to the world monetary system but it did not find any reflection in the new statutory provisions for SDR's because of the vigorous resistance offered by the industrialised countries. Since agreement has been reached on the SDR system and the supplementary IMF agreement has been passed, the campaign in favour of the link has however gained in intensity, not only in the developing countries but in the industrialised countries as well. Essentially, the following arguments are adduced as justifying the link:

☐ According to the present criteria for the distribution of SDR's (IMF quotas) the developing countries receive only about 28 p.c. of all SDR's.

☐ Owing to their unfavourable export structure, high investment needs and the food imports necessitated by more frequent crop failures, the LDC's require a relatively higher degree of liquidity than the industrialised countries.

¹ International monetary reform and co-operation for development, Report of the Expert Group of International Monetary Issues, United Nations, New York, 1969.

☐ National budgetary difficulties arising when development aid is increased can be obviated by the transfer of SDR's. The link is therefore a suitable vehicle for raising development aid towards the 1 p.c. target.

☐ There is no adequate access to the international capital markets and to bilateral balance-of-payments assistance for LDC's at present.

The views on the volume of SDR's to be surrendered by the industrialised countries range from 25 to 75 p.c. of their national allocations; 50 p.c. is mentioned most frequently as a figure for purposes of illustration. On the basis of the first decision on SDR allocations, which was for \$9.4 bn consisting of \$3.4 bn on January 1, 1970, and \$3 bn in each of the following two years, the total amount could, in absolute terms, vary between \$750 mn and \$2.5 bn a year.

The reason given for these large demands is that they offer the only chance of attaining in the near future the 1 p.c. target which is aimed at and was pledged by the industrialised countries. The total development aid by western industrialised countries belonging to the DAC amounted in 1968 to \$13 bn, including \$6.4 bn of public assistance, or 0.77 p.c. of their GNP of \$1,700 bn. The development aid would thus have to be increased by 0.23 p.c. of GNP, i.e., by \$4 bn, in order to reach the 1 p.c. target.

The Attitude of the Industrialised Countries

The industrialised countries were able to fend off the link when the SDR system was under preparation. Under the IMF Article of Agreement the World Bank and IDA are not permitted to hold any SDR's. The uncompromising attitude of the industrialised countries was made clear again at the World Trade Conference as well as the annual IMF meeting in Copenhagen. The industrialised countries therefore did not deem themselves able to accept No. 52 of the Strategy Document either and lodged formal objections to it.

The argument so far presented against the link are, essentially, concentrated on the following points:

☐ The SDR system has been designed to satisfy the need of the individual countries for "reserves to hold" and not for "reserves to spend". The SDR's and the IMF should not be encumbered with tasks of development policy with which they were not originally intended to cope.

☐ Development aid demands a constantly expanding supply of long-term capital which should not be subject to possibly wide fluctuations and interruptions when new SDR's are created.

☐ Inauguration of the link would establish on the world scale a new principle for the raising of funds which enables development aid to be given through international money creation and does not presuppose voluntary restraint on consumption and investment in the donor countries. The objections which must be raised against financing domestic tasks within a State by creation of money apply with even greater force to such backdoor financing in the sphere of international tasks.

There is a danger of excessive reserves being created under pressure by the developing countries, with the long-term consequence of loss of confidence in this new reserve medium and an increasing inflationary potential in the world.

In the industrialised countries, as in the developing countries, there has for some time been no full consensus on the question of the link. The differences are however, in the present phase of the discussion, confined to the question of the appropriate tactical approach to the problem. While some countries express themselves in favour of an investigation of the link by the IMF, the overwhelming majority of the industrialised countries are against a formal investigation into the link on the part of the IMF because this could only raise unjustified hopes in the developing countries.

In view of the existing differences between industrialised and developing countries the IMF has been very cautious in its pronouncements. The Managing Director of the Fund, Mr Schweitzer, avoided in his concluding address in Copenhagen giving a promise of an investigation into the link by 1972, but he pointed out that the Executive Directors would give careful attention to the IMF working programme in this field.

A Compromise is Possible

The negative attitude of the industrialised countries to the financing of development aid by a redistribution of SDR's does not mean that they do not appreciate the particular liquidity requirements of the LDC's.

On various occasions the developing countries have already received a larger portion of international liquidity than would be their due under the so-called Bretton Woods formula which comprises changes in national income, currency reserves and exports and imports among the criteria determining the share of individual countries. On the strength of the IMF decision of 1963 concerning compensatory financing of shortfalls in export proceeds, for instance, a number of quotas of primary producing countries have been selec-

tively raised and thus the scope for IMF credits to them enlarged. When the quotas were increased last, in 1969, the industrialised countries similarly accepted smaller additions to their quotas than they were entitled to by calculations according to the Bretton Woods formula, with consequent benefits for the developing countries. The IMF has also made allowance for the special liquidity requirements of the primary producing countries within the compass of its drawings policy by conceding to these countries

SDR's to offset shortfalls in export proceeds and to finance payments to international commodity buffer pools.

When the decision was taken on the rules for the election of directors in 1970, the IMF promised to undertake a study to examine the quota structure and vote distribution in the IMF. In this context the IMF Board will have to concern itself again with the question of securing a satisfactory share in the international liquidity supply for the LDC's.

The World Commodity Markets in 1970

by Heinz Kolbe, Hamburg

Price trends on the world commodity markets have been far from uniform in the course of 1970. The food prices rose from December 1969 to December 1970 on average by no less than 8 p.c. After years when in some markets supply greatly exceeded demand, production has latterly scarcely kept up with requirements with the result that it is feared that shortages will develop in the not too distant future. In the world markets for industrial raw materials, on the other hand, the slowing down of boom conditions everywhere led from May 1970 to a steady decline of prices on a broad front. In the twelve months from May 1968 until May 1969, the level of prices for industrial raw materials had risen by 18 p.c. in consequence of the boom conditions in the Western countries and as a result of particularly heavy raw material purchases by the Eastern Bloc states. Since May 1969, prices have again steadily receded, however, by 5 p.c. In the course of the past year—from the end of December 1969 until the end of December 1970—price levels actually declined, however, by no more than 3 p.c., the relatively small loss being due to the rises that had taken place during the early part of the period, i.e. until May. In fact, the annual average for 1970 is even 5 p.c. higher than that of 1969. This is due to the difference between the state of affairs as it existed at the end of 1969 and the average for the year.

Market Trends

Since spring 1970, non-ferrous metals and steel have become cheaper in the export markets. The

downward trend for rubber and wool, which had already set in earlier, continued for most of the time, with the exception of the last few weeks. On the other hand, prices for cotton and fuels—partly influenced by special factors—have risen. On the food markets supply shortages led to price increases for sugar, coffee, oilseeds and vegetable oils. 1970 also witnessed higher prices for grain, meat and dairy produce, whereas cocoa quotations, after soaring for two years, registered a marked decline.

The rise in world market prices since 1968 was from the export earning's point of view of the typical producer-countries as for instance the developing countries all the more important as the industrial products which they import became dearer at the same time. For the industrial countries, on the other hand, the boom prevailing on the commodity markets was a considerable cost factor which accentuated the strong general upward price trend. By contrast, the more recent decline of the prices for industrial raw materials is now having a most welcome effect inasmuch as it helps to damp down the tendency for prices to rise. But there is a reverse to the medal: the lightening of the industrial countries' burdens means on the other hand losses for the developing countries. True, the latter had previously been able to stock up their foreign exchange reserves so that they should be able to increase their imports for some time yet even if the deterioration of the state of the export markets should result in smaller revenues from their exports.