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On one point however the arguments of those against the "link" are not so easily dismissed; it is this: Too liberal a creation of SDRs, possibly even through a basic change in the majority situation in the IMF, may offend against the scarcity principle to which in the last resort every kind of money owes its ability to function. It may indeed be possible that for technical reasons a mixing up of monetary policy with development aid proves to be inadvisable. But such technical

reasons should not blur the basic idea that new ways of transferring resources must be found, if development policy is to remain effective and credible. This is why it is well worthwhile thinking carefully whether international credit creation could not be used for purposes of development aid. The conditions should be such as to permit the young countries to build up a strong infrastructure without for ever feeling the iron hand of their creditors closing round their necks.

Special Drawing Rights and Development Aid

by Dr Dietrich Kebschull, Hamburg *

The introduction of the Special Drawing Rights (SDRs) has not fulfilled the wishes of the LDCs. Whereas the industrialised countries look upon SDRs simply as international liquidity reserves, LDCs aim at the linking of SDRs with development aid. Is their concept really as out of place as the industrialised countries maintain it is?

The industrial countries which have command over the absolute majority in the International Monetary Fund (IMF) utilise the SDRs in accordance with their own requirements. In their view the SDRs are meant to serve two main purposes:

☐ To satisfy the liquidity requirements of the great trading nations, continuously growing, as they do, in the wake of world trade expansion. (In this context the SDRs are of particular significance because they do not only represent additional reserve media aside the traditional reserves but are also meant to offset the declining importance of the pound, the dollar and gold.)

☐ To counter-balance short-term balance of payments deficits which, at growing volume of a country's foreign trade, necessarily appear more often because of the time gap between the flows of goods and the flows of capital.

Restricting Regulations

For the purpose of upholding the reserve criterion and, at the same time, to safeguard against any undue deployment and creation of SDRs, the obligation of reconstitution was introduced. It entails the duty that, five years after the first allocation and thereafter at the end of each quarter, a total of at least 30 p.c. of the allocated SDRs must — in spite of prior utilisation — have been reconstituted. The aim of this direction is the avoidance of SDRs

being used as reserves under balance of payments aspects and, in the extreme, exclusively for the financing of imports.

In order to avoid an exaggerated creation of SDRs, the EEC countries also made sure of a blocking minority. 85 p.c. of the IMF votes are necessary before new SDRs can be created. The EEC countries among them have 16.2 p.c. of the votes.

Demands of the LDCs

The allocation of SDRs is based on present IMF quotas. According to the LDCs the SDRs and their allocation system fall short of their special requirements. The LDCs are less concerned with reserves to combat balance of payments imbalances but rather with additional financial means to be put at their disposal by the industrialised countries.

In order to obtain more capital for development purposes they emphatically demand a link between SDRs of the developed countries and development aid. There are two different basic patterns in the propositions for such a link:

☐ A part of the industrial countries' SDRs is to be put at the disposal of the International Development Agency (IDA) after the allocation by the IMF. IDA subsequently exchanges these SDRs into the currency of the relevant industrialised countries and

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utilises the funds thus accumulated for the financing of development projects (direct link).

☐ The industrial nations initially take the SDRs themselves but, in the second phase, place a certain percentage of them at the disposal of IDA in their own currency (indirect link).

There are various conceptions of the percentage to which the LDCs should participate in this manner in the industrialised countries' SDRs; they reach from 25 to 75 p.c. (The question of the reconstitution does not altogether come out clearly in the link-concepts. As far as the reconstitution principle is to be upheld, IDA should be responsible for this aspect).

Possible Effects of the Link

The propositions for the direct and the indirect link are rejected by the developed countries (for instance Japan, Canada, France, Belgium, the Federal Republic of Germany) on the strength of three main arguments:

☐ The link will lead to equal interests of LDCs and industrialised countries with permanent balance of payments deficits. Those countries will, in common, time and again urge the creation of additional SDRs.

☐ The link will facilitate the utilisation of the artificially created SDRs towards import financing. This would entail the danger of a world-wide inflationary process.

☐ The utilisation of SDRs for development financing would infringe upon their criterion. The industrialised countries' opinion is that SDRs are not "reserves to spend" but "reserves to hold".

Even in industrial countries these arguments meet with increasing criticism. Leading scientists such as Tinbergen, Streeten or Machlup speak of possibilities to realise the link.

Controllable Creation of New SDRs

It can be said at the outset that the often-feared uncontrolled creation of SDRs is hardly likely ever to occur. After all, the IMF creates new SDRs only in accordance with international liquidity requirements. These requirements, in turn, result from the declining significance of traditional reserve media and the impact of growing world trade. It is admittedly not possible to assess these requirements precisely, but one can estimate them. Internationally the IMF is in a situation similar to that of a national Central Bank which has to adjust the money volume to the growing national product or

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V E R L A G W E L T A R C H I V G M B H - H A M B U R G

higher transactions in its economy, respectively. The past has shown that the relevant institutions are well in the position to master this task.

Whereas, in this field, the IMF's experience with the creation of additional SDRs may serve as something of a guarantee against overstepping the creation of SDRs, this danger is almost altogether eliminated through the necessary 85 p.c. majority of IMF votes. The often-feared "unholy alliance" between developed deficit countries and LDCs is, judged on the voting structure, scarcely possible at all because all industrialised nations and all LDCs will probably never follow a common policy in this respect. The Federal Republic of Germany and Great Britain alone could, on the strength of their voting share of 15.22 p.c., prevent the issue of new SDRs.

The EEC in its present shape is already in a position to prevent an over-liquidity by means of the creation of new SDRs. The progressing European integration and the efforts towards a currency union speak for the expectation that in future the EEC countries will act, and cast their vote, much more uniformly than before. The breaking-out of line by one or more than just one EEC country with balance of payments deficits and a resulting coalition with the LDCs and all deficit countries will then become near enough impossible.

Danger of Inflation Exaggerated

These deliberations show that any judgement of the effects of the link will always take into account several different aspects. This also applies to the alleged danger of inflation because of the link. The very circumstance that additional SDRs are foremostly created according to international liquidity requirements and that their creation can be controlled by the IMF allows by and large for the exclusion of inflationary trends through over-supply of international liquidity. In the eyes of the link opponents there is, however, another weighty source of inflation, namely that the LDCs utilise the SDRs, obtained through the link, for the financing of imports from industrialised countries. They assert that the thus possible additional demand would be reflected chiefly in internationally highly competitive countries whose capacities are already distinctly stretched. But this generalised argument cannot be upheld:

☐ The demand from LDCs is not solely price-orientated. In the field of the import of capital goods particularly former contacts with certain industrial nations, previous supplies, service performances, quality or conditions of payment (mainly for complementary deliveries), etc., strongly influence the purchasing decision. The de-

mand may therefore also be directed to countries in a short-term phase of recession (and, because of this, have a positive effect on such a country's economy).

☐ The size of the demand stemming from a link relativates the danger of inflation strongly even if and when the demand would actually be directed exclusively to industrialised countries with a booming economy. During the period 1970–1972 a total of 9.5 bn SDR units (1 unit = 1 \$ at the old parity) are to be allocated. The third allocation, on January 1, 1972, amounted to about 3 bn. On the assumption that of this total industrialised countries will receive approximately 2 bn, something between 500 mn and 1.5 bn will go to the LDCs under the link (disregarding reconstitution, and based on a link of 25 p.c. and 75 p.c., respectively). On the basis of old dollar parities this sum would represent 3.2 p.c. and 9.7 p.c., respectively, of the development aid performances of the DAC countries in 1970.

In the event of the entire additional demand potential being directed into Germany, the result would be an additional export of 1.5 and 4.5 p.c., respectively (based on Germany's export in 1970). But in view of the fact that the additional demand would be distributed among all developed countries, the corresponding export growth could hardly be regarded as furthering inflation.

Counter-Actions Possible

Even if the export growth should be substantial, there are possibilities in the industrialised countries to pursue a corresponding anti-inflationary policy. This is being done already by nearly all developed countries today in order

- ☐ to use further the export as a growth factor;
- ☐ to dampen the tendency to inflationary effects of credit-financed deliveries, resulting from private aid, in LDCs;
- ☐ to neutralise publicly financed aid, which partly stems from credit creation within the budget, in respect of its effects on the level of prices.

In the course of the inflation discussions it will moreover be necessary to go into the question as to whether the additional demand created by the link would in fact enhance the development volume to the same extent. With a certain degree of likelihood it can be assumed that this will not be the case because

- ☐ the link performances will be accounted for within the one-p.c.-clause;
- ☐ they substitute the former public performances at least partially.

The already limited inflationary effects of the link will thus have to be reduced by the inflationary effect of the substituted transactions.

The role of IDA is totally overlooked in almost all arguments against the link. This institute, however, acts as supplementary regulator. After all, the SDRs are not put at the LDCs' disposal but remain at IDA. Going by the present plans one can take it that IDA will deploy the link-means for the financing of its development projects. The usual scrutiny and methods of evaluation provide the possibility for the taking into account particularly the development efficiency (for instance consideration of the least developed countries). A certain regional steering of the capital flows seems realisable.

Little Influence of the LDCs

So far it is not clear whether IDA, with the aid of the SDR projects, finances on the basis of credits or grants. But it can be assumed that IDA adheres to its business practice of very long-term and free-of-interest credits. In respect of the inflationary effect there are, however, no great differences between credits of this nature and outright grants. The link has no inflationary effect on the LDCs themselves. While in the LDCs the domestic supply will be stepped up, the money flows will not be directly influenced.

Leaving the discussion about inflationary effects aside it can be said about the differentiation between "reserves to hold" and "reserves to spend" that this sub-division is rather an arbitrary one. In the last resort all reserves are accumulated for the purpose of being spent at some time or other.

Discussion Necessary

It appears more important than this classification to look into the question as to whether or not the functional capability of the SDRs would be impaired on account of the link. On the strength of the above deliberations there is little likelihood for this to be the case as long as the basic rules for the creation of SDRs are upheld.

As a control over the creation of SDRs is obviously possible, the inflationary effects appear considerably smaller than heretofore suspected and as, lastly, there are, within IDA, additional institutional control possibilities, it does seem purposeful for the industrialised countries to reconsider their present rejecting attitude towards the link, and do so mainly under the aspects of development policy. No good service will be done for the development policy if one were to stick to the rigid "No" also in Santiago.

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by Ernst Niemeier

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Octavo, 250 pages, 1970, paperbound, price DM 34.—

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