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SDRs, the IMF and the Future

In principle, the general climate for the 49th annual meeting of the International Monetary Fund (IMF) and the World Bank in Madrid was a propitious one: the world economy and world trade are filling their sails and the Western industrial countries would seem to have weathered the recession, though the cold winds of rising interest rates worldwide are blowing hard into the faces of those fiscal policymakers charting the ship of government through high indebtedness and budget deficits, i.e. fiscal policymakers nearly everywhere.

But satisfaction with economic developments, registered by the Western industrial countries at least, was marred by the dispute over the general allocation of Special Drawing Rights (SDRs) demanded by the IMF amounting to 36 billion SDRs. The rationale for this replenishment of IMF funds is that since the last general allocation in 1981 – which did not just accidentally happen to coincide with the onset of the debt crisis in many developing countries and the attendant threat of a collapse of the international financial system – the IMF has gained 38 new members that have so far received no Special Drawing Rights. The sum which would be required for an “equitable allocation”, however, is estimated at a maximum of 16 billion SDRs. The reason the IMF gives for the additional injection of some 20 billion SDRs is the so-called “global need” for currency reserves.

The representatives of the industrial countries in the Group of Seven (G7) and in particular the German Bundesbank were prepared to agree to a stocking up of the SDR pool to ensure the equitable treatment of the new IMF members, but they turned down the additional allocation, arguing that there is no evidence of a long-term global need for the creation of additional liquidity. In response, the representatives of the developing countries organized in the Group of 24 not only rejected the more modest option but also the extension of the IMF's Systemic Transformation Facility (STF), which supplies members with resources when traditional trade and payments relationships are seriously disrupted due to the transition from a centrally planned to a market economy. Although after the (non-)outcome of the Madrid conference the STF will expire at the end of 1994, the second tranches of drawings already approved can still be disbursed until the end of 1995. Thanks among other things to this time span, it is not surprising that the IMF's Managing Director, Michel Camdessus, is optimistic that an agreement can be reached on the increasing and allocation of SDRs by spring 1995.

Perhaps the tug-of-war over the “artificial money” which the Special Drawing Rights represent is not crucial compared with general agreement that the anticipated 3.5% global growth in 1995 should be put to “wise use” (Camdessus) in order to make the recovery sustainable and avoid the mistakes made in the last upswing. Perhaps the rejection of a partial increase by the G24 can be interpreted as an “uprising of the Davids” against the powerful in the international monetary system; perhaps the failure to arrive at a partial solution in favour of the new members and the refusal to prolong the Systemic Transformation Facility can be interpreted as the first shots in a battle between the traditional developing countries and the new members from Central and Eastern Europe and Asia for scarce resources. Perhaps the Managing Director of the IMF is right when he claims that an increase in the stock of SDRs of the size which he has

proposed will not cause inflation, among other reasons because the entire volume of SDRs currently makes up only some 2% of global reserves.

Nevertheless, given today's basically freely fluctuating exchange rates and free capital movement, can we assume a "long-term global need" for more SDRs? Generally, currency reserves are only needed to finance current account deficits where foreign capital cannot be attracted due to adverse local general economic conditions and the achievement of a balance via the adjustment of exchange rates, i.e. devaluation, is ruled out. In other words: by using reserves, the necessary economic policy adjustment can be deferred, or at least prolonged.

The allocation of Special Drawing Rights thus amounts to nothing other than diluting the control by the financial markets over the economic policy of individual governments and conferring more control on the IMF. That this may well be in the interests of the IMF as an institution is understandable. Whether the IMF is able, however, to exert more effective control over economic policy in the various countries than the international financial markets is a moot point not only considering the political sensitivity of the dialogue between the IMF and the governments concerned but also in view of the policymaking process within a country amongst the various parties and interest groups. This explains why the President of the German Bundesbank, Hans Tietmeyer, stands at the forefront of those opposing a further allocation of Special Drawing Rights beyond the "equal treatment" requirement and logically demanded in his speech to the Board of Governors that the IMF return to its function as a straightforward monetary institution.

Against the background of open capital markets and fluctuating exchange rates this function cannot be restricted, as it was in the era of the Bretton Woods system, to financing its members' balance of payments deficits, which could be considered temporary either from the outset or after the implementation of structural adjustment measures. Fluctuating exchange rates and liberalized international capital markets can undermine the sovereignty of domestically oriented economic policy. The development of exchange rates is crucial for economic policymaking in the various countries, as the real exchange rate determines the level of real income and assets in relation to other countries. It is therefore arguable in the broadest sense that economic policy under the conditions of fluctuating exchange rates must look to prevent unnecessary changes in real exchange rates. As, though, it is in the nature of exchange rates that they are not subject to the decisions of single nations, it may be inferred that this is not the job of national economic policy but falls under the auspices of the concerted economic policy of several countries. Although one should not overestimate the scope of policy coordination, the IMF could act here as a forum for the avoidance of economic policy clashes. At least amongst the member countries this function is not in dispute. In view of the liberalisation of capital markets and in particular of the new financial instruments and derivatives, it could also act as a global watchdog for these markets.

Spending even more money on medium-term and long-term funding of structural adjustment in developing countries and countries in the process of transforming their economic systems fits badly into this profile. The overlap between IMF and World Bank operations would only increase. The closer cooperation between the two institutions that this would entail might be seen as a welcome development, bearing in mind that apart from "cross conditionality" this could result in a certain adulteration of the areas of competence on both sides. This adulteration, in turn, could also mean that certain major donor countries might be tempted to make use of the greater leeway afforded by this overlapping of competence to manipulate the institutions, depending on their own influence (the IMF is traditionally headed by a European and the World Bank by an American), to their own foreign policy and economic advantage. If closer cooperation between the World Bank and IMF is nevertheless to be achieved, at some point in time a thorough demarcation of responsibilities will have to be made. It remains to be seen to what extent the involvement of both institutions in the former socialist countries of Europe will lend impetus to this process.

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