Frequently Asked Questions
On Special Drawing Rights

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What are SDRs?

Special Drawing Rights (SDRs) are a financial asset created by the International Monetary Fund (IMF) for its 190 member states. They are meant to be used as reserve asset to meet external financing needs.

In simple terms, ‘reserve assets’ can be understood as the balance on a country’s current account. It is the foreign exchange cash that the central bank has at its disposal to satisfy the government’s, corporations’, and individuals’ demand for foreign goods, services and assets. The balance should not go too low, or else the country could face a balance of payments crisis: no foreign cash in the coffers to pay everyday bills. Reserve assets consist of hard currencies, gold, the country’s reserve position at the IMF, and SDRs (Figure 1).

Figure 1. World’s total reserves

SDRs are like a credit card that a bank (the IMF) issues to all its customers (its member states), with a credit limit equal to each customer’s deposits (IMF quota), a uniform interest rate based on the highest credit score (the credit rating of five rich countries), and a minimum monthly payment equal to the interest charge (no deadline to reimburse the money drawn on the SDR card, but an obligation to pay interest as long as you do not reimburse it).

More technically, SDRs are an asset with which central banks can buy each other’s hard currency holdings, specifically US dollars, euros, British pounds, Japanese yen and Chinese yuan. The IMF can allocate SDRs to all its members in proportion to their

quotas, which are the basis of both contributions to and voting rights at the IMF. A small number of international institutions called ‘prescribed holders’ can also hold and trade SDRs for hard currencies, but do not receive an allocation. The IMF settles the exchanges of SDRs for hard currencies by maintaining a SDR account for each country and prescribed holder. Countries can buy, sell, lend or swap SDRs for hard currencies as they wish. When a country wants to sell SDRs that no one wants to buy, the IMF can ‘designate’ (i.e. force) a country that has plenty of hard currencies to buy those SDRs. In practice, designation has not been used in recent decades. Countries receive an interest rate on the SDRs they hold and pay the same rate on the SDRs that they were allocated.

There is no obligation to buy back the SDRs that were sold (i.e. to return the hard currencies that were bought). However, as long as a country does not buy back the SDRs it sold, it will have a negative balance on its SDR account (lower holdings than cumulative allocations) and will be a net payer of interest. Conversely, countries that ceded their hard currencies to buy SDRs gain interest for as long as they maintain a positive balance on their SDR account. The interest rate is set at a weighted average of the interest rates for three-month treasury bills of the five underlying currencies. Likewise, the value of one SDR equals the value of a basket of the five currencies, with weights corresponding roughly to the relative sizes of the corresponding economies. The SDRs’ exchange rate is adjusted on a daily basis and the interest rate on a weekly basis based on the five underlying currencies’ exchange and interest rates variations on international financial markets. One SDR is currently worth about US$1.32.4

**What Is the process to create SDRs?**

According to its Articles of Agreement, the IMF management must assess during every ‘basic period’ (set by default at five years) how many SDRs to allocate in order to satisfy the global demand for reserve assets, which naturally grows as the global economy grows. An 85 percent majority vote of the IMF board is then needed to approve the allocation. The current basic period (the twelfth) runs from calendar 2022 to 2026. The allocation can be distributed in one go or by annual instalments.

As the United States holds about 17 percent of the votes, it has a veto right. According to US law, allocations to the United States adding up to more than the US quota at the IMF within the basic period must be approved by the US Congress. That cap was worth about US$650 billion at the time of the last allocation in 2021, and is currently about US$630 billion (because of exchange rate variations). The IMF board approved an equi-proportional quota increase of 50% in December 2023. If the US Congress approves the US contribution to that increase, it will bring the cap to around US$945 billion.

The IMF board can also shorten the basic period, or it can start a new one ahead of time when it assesses that there is an ‘unexpected major development’ (i.e. a crisis). However, the purpose of SDRs is to satisfy the global, long-term needs for reserves.

The IMF board can also cancel SDRs if it assesses that there is a global liquidity glut, which would require all countries with negative balances on their SDRs account to sell hard currencies. This also requires an 85 percent majority and has never happened.

Changing these rules by amending the Articles of Agreement not only requires an 85 percent majority at the IMF board, but in many countries must also be ratified by the legislature.
What are the benefits of SDRs?

SDRs have multiple benefits:

1. They are valuable even when they are not used, as they bolster market confidence in the currencies of the countries that hold them. They are an additional and cheap lifeline in case of crisis, as the central bank can exchange them for hard currencies to defend the value of the national currency if need be.

2. Just as you can afford to save less and maintain a lower balance on your current account when you know that you have a low-rate credit card to cover unexpected bills, SDRs are a substitute for the accumulation of hard currency reserves through national savings (e.g. exporting more than importing).

3. In some countries (depending on national law) central banks can transfer SDRs to the government’s budget to be spent on national priorities.

For low-income countries, selling their SDRs for hard currencies is a very cheap form of capital because they get the interest rate of AAA-rated countries even when their own credit ratings are in the doldrums, and they get to pay a short-term rate on a perpetual (i.e. indefinite) loan.5

For high-income countries, and especially for countries issuing reserve currencies, SDRs are less valuable, just like when your bank raises your credit card limit when you already have plenty of cash in your current account. But they are still nice to have. In practice, rich countries also cash in their SDRs from time to time, as part of normal treasury management at the central bank (just as a multinational corporation would move money between its dollar and euro current accounts depending on expected bills and prevailing interest rates and exchange rate expectations).

What are the costs of SDRs?

As long as they are not converted into hard currencies, SDRs do not cost anything to anybody, just as an unused credit line does not cost anything.

Countries that do convert SDRs into hard currencies incur a low interest charge until they pay the hard currencies back (which they do not have to do).6

To whom do SDRs belong?

According to the IMF’s Articles of Agreement, SDRs are allocated to its “members”, i.e., states. That means that national governments can dispose of them as they wish. In a few countries including the USA, United Kingdom and Japan, SDRs are managed by a dedicated foreign exchange fund controlled by the Finance Ministry. In most countries, however, SDRs are managed by the central bank. That has led to some confusion as to the level of control of governments (as opposed to central banks) over them. The bottom line is that it is a matter of national law. If needed parliaments can change the law to empower governments to dispose of SDRs at their discretion.7

SDRs are distributed to IMF members in proportion to their quota, which are the basis of both contributions to and voting rights at the IMF.8 Hence high-income countries
get a lot of them, and low-income countries little, although they represent a larger amount relative to the latter’s GDP or reserves.

Are SDRs a global currency?

No. Only a handful of institutions hold SDRs and the only thing they can buy with them are dollars, euros, pounds, yen or yuan.

However, one might say that SDRs are a proto-global currency, as they fulfil the three purposes of money, but only in a very restricted way:

- Unit of account: SDRs are only used as a unit of account by the Bank for International Settlement (BIS) and partially by the IMF, UN agencies and some other international institutions.
- Means of exchange: SDRs are only exchanged among central banks and a few international institutions.
- Store of value: SDRs are only held as a financial asset by central banks and a few international institutions.

Are SDRs debt?

Once used, SDRs must not be repaid, hence some commentators consider them a debt-free instrument. However, they do involve an obligation of future payments: the interest charge. For economists, they are a perpetual loan: a debt with undefined maturity, that can be repaid whenever the borrower wants and that incurs an interest charge as long as it is not repaid.

For accounting purpose, the IMF’s Balance of Payments Manual recommends central banks to record SDRs as both asset and debt. When they are used, the asset is converted into a hard currency asset, while the debt persists. However, the previous version of the Manual recommended to record them as asset and equity instead of debt. This distinction has legal implications, as national laws usually impose more restrictions on the use of debt than equity. The IMF should revert back to its former recommendation. That said, the recommendation is not binding, and governments can change national laws to account for and use SDRs as they wish.

Note also that the IMF can cancel (i.e., recall) SDRs, in which case used SDRs must be repaid. Although that may be interpreted as giving them more of a debt character, equity can also be cancelled through capital reductions. SDRs have never been cancelled and are unlikely to be.

Do SDRs cause Inflation?

No. SDRs can theoretically increase inflation in reserve currency-issuing countries only when they are exchanged for hard currencies. However, SDRs allocations have had no measurable impact on global inflation. The amounts exchanged in the months following the 2021 allocation represented only 0.4% of the money creation by rich countries’ central banks between March 2020 and April 2023. Moreover, rich countries follow a monetary policy to meet a certain level of inflation and will reach that target by adjusting interest rates, regardless of SDR allocations.
Do SDRs cause unemployment?

No, to the contrary, they can decrease unemployment. SDRs give countries breathing room in their balance of payments to stimulate their economies to recover from crises or when there is an output gap (i.e., when actual production is lower than capacity).

Reserve currency-issuing countries also benefit when the rest of the world use their SDRs to stimulate their economies, as that drives up demand for the former’s exports.¹³

What is the origin of SDRs?

SDRs were created in 1969 to complement gold and the US dollar as reserve assets. During the dollar standard era (1945–1971), countries maintained a fixed exchange rate (with occasional devaluations) between their currencies and the US dollar. The dollar’s value was itself anchored to gold: it was convertible at a fixed price of US$35 for an ounce of gold. Since exports of goods, services and capital do not equal imports, central banks needed to buy and sell dollars constantly to maintain the fixed exchange rate. They needed to build a cushion of dollar reserves for that purpose, which required the United States to run a balance of payments deficit: dollars needed to flow out of the United States through trade, aid and foreign investments. The United States was allowed to run a long-term balance of payments deficit because the rest of the world was willing to accumulate dollar reserves.

As global trade grew, so did the dollar reserves of central banks around the world, which by 1964 surpassed the US monetary gold stock.¹⁴ Convertibility was threatened, and US authorities faced the so-called Triffin Dilemma: either they let the US balance of payments deficit run amok, in which case the dollar would become increasingly overvalued and the risk of a dollar run grew;¹⁵ or they adopted austerity measures to cut the US balance of payments deficit, causing a recession in the United States and also harming growth in the rest of the world, as there would no longer be sufficient liquidity (i.e. dollars) to let trade and foreign investment thrive. Neither option was palatable to anybody. SDRs were thus created by consensus as an additional reserve asset to let central banks continue to accumulate reserves without increasing either dollar reserves, which would have required ongoing US deficits and further undermined confidence in convertibility, or gold, of which the supply is naturally limited.

Why did SDRs almost fall into oblivion?

SDRs came too little, too late: the risk of a dollar run grew in the late 1960s and in 1971 President Nixon unilaterally ended the convertibility of dollar into gold. The dollar devalued and European countries abandoned their fixed exchange rates against it in 1973. The 1960s and 1970s also witnessed an expansion of global finance thanks to deregulation and technological progress. Money started flowing across borders not just for bricks-and-mortar foreign direct investment, but also for portfolio investment and short-term speculation. This is important because economic theory demonstrates that it is impossible to have a fixed exchange rate, completely free cross-border capital movements, and an independent monetary policy to boost a country’s growth and curb inflation, all at the same time. During the dollar standard era, exchange rates were fixed (but with a growing number of devaluations in the 1960s) and countries could conduct independent monetary policy, but capital
movements were repressed (though increasingly relaxed during the 1960s). In the
1970s, the prevailing view among economists continued to be that fixed or at least
managed exchange rates were important, which explains why, despite the collapse of
currencies’ pegs to the dollar, there was continued support for large reserves and
hence for SDRs. After the initial SDR allocation of 1970–1972, a second was
approved for 1979–1981. In 1978 a provision was even enshrined in the IMF Articles
of Agreement to make SDRs the principal reserve asset.

However, with the Reagan Administration the international monetary system took a
definitive turn toward flexible exchange rates. Private capital could flow freely across
the main economies, monetary policy aimed at domestic objectives of growth and
inflation, and as a result the value of the dollar swung widely throughout the 1980s.
The flexible exchange rate regime persists to this day. Reserves, and hence SDRs, play
a less important role in a flexible exchange rate regime, as differences between
exports and imports make the currency appreciate or depreciate, which drives capital
flows in or out to bring the balance of payments to equilibrium, without the need for
the central bank to buy or sell a lot of reserves. This is a major reason why interest in
SDRs diminished. Central banks have continued holding dollars, with a partial
diversification into euros and, to a lesser extent, pounds and yen. Countries that let
their exchange rate float and can use their own currency to pay for imports (because
the exporter is willing to hold that currency as a reserve asset) can afford low
reserves.

**Why are SDRs still relevant in today’s international monetary system?**

We are far from a pure flexible exchange rate system. Beyond the four main hard
currencies (dollars, euros, yen and pounds) and a few others, many countries
continue to manage their exchange rates, which requires more reserves. Some
countries purposefully accumulate reserves to maintain low exchange rates in order
to boost export-led growth strategies. As a result, they run long-term balance of
payments surpluses and keep hoarding more hard currencies. The 1997 financial
crisis in Asia also led several Asian countries to accumulate ample reserves to protect
themselves against another balance of payments crisis. Together, this explains why
the countries with the most reserves are not necessarily the largest economies (see
Figure 2)

*Figure 2: Top 20 countries and territories by reserve holdings*
The Triffin Dilemma remains relevant in this imperfect flexible exchange rate system. The prevalence of large trade surpluses in some countries in order to build up precautionary reserves necessitates the existence of large trade deficits in reserve currency-issuing countries. The case for more SDRs from the perspective of non-reserve currency-issuing countries is thus to acquire sufficient reserve assets to weather crises without the need to run trade surpluses (i.e. producing more than consuming) or borrowing from financial markets (which is expensive). Reserve currency-issuing countries don’t have an interest in running deficits over the long term either, as it builds up unsustainable debt. From both perspectives, more SDRs would enable smaller macroeconomic imbalances and more global economic and financial stability.

Notes

1. The term ‘balance of payments’ is here used at the exclusion of changes in the central bank’s reserves. It equals exports minus imports of goods and services (i.e. the trade balance), plus receipts minus payments of cross-border income (e.g. interests) and transfers (e.g. remittances and aid) – all of which equals the ‘current account’ – plus acquisitions (net of sales) of domestic assets by non-residents (e.g. external borrowing by the government, foreign direct investment of multinationals in the country), minus acquisitions (net of sales) of foreign assets by residents (e.g. rich individuals’ bank accounts in Switzerland). If the sum of all these cross-border monetary flows is positive, the central banks’ reserves increase; if it is negative, they decrease.

2. IMF members can withdraw part of their quota (i.e. the capital they paid in to become a member) in a balance of payments crisis, without incurring interest.

3. Thanks to Ted Truman for this analogy.


9. The BIS is the ‘bank of central banks’. Based in Basel, Switzerland, it is owned by central banks and provides them with financial services. It also serves as a forum to coordinate banking regulations.


15. US$35 per ounce was the price at which the US Federal Reserve guaranteed it would exchange its gold for foreign central banks’ dollars. There was a parallel private market for gold. When the price on the private market significantly exceeded US$35, there was a risk that central banks would convert their dollars for the Fed’s gold at US$35, then sell that gold on the private market.