POLICY BRIEF

Reforming SDR Allocation Criteria to Enhance its Role in Global Crisis Response and Sustainable Development Financing

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Financing for Sustainable Development

Abstract

Emerging Markets and Developing Economies (EMDEs) face acute financing constraints due to elevated debt burdens amidst growing development and climate-related needs. The structural asymmetries of the international monetary system exacerbate these challenges, particularly through pro-cyclical capital flows toward EMDEs that lead them to accumulate reserves for precautionary purposes. Special Drawing Rights (SDRs) offer a concrete alternative to address these asymmetries and financing needs. However, its current design and allocation system pose challenges. In this policy brief, we focus on the ones related to SDR allocation criteria and propose some guidelines and concrete alternatives on how this could be reformed to harness the use of SDRs for crisis management and financing for development. The current allocation mechanism largely favours advanced economies – countries that neither need nor significantly use SDRs. Therefore, we propose a needs-based approach that incorporates metrics of financial and structural vulnerabilities. While acknowledging the political challenges of such reform, the brief outlines recommendations for designing a technically feasible and transparent allocation framework.

Keywords: Special Drawing Rights, International Monetary System, Financing For Development

Diagnosis

Many Emerging Markets and Developing Economies (EMDEs) face elevated financing needs coupled with high debt burdens and interest rates. Due to high-interest costs and growing external debt service burdens, there has been a crowding out of growth-enhancing development spending[1]. Furthermore, the decline in net external flows,[2] the limited access to concessional financing for low- and middle-income countries[3] and the necessity to address climate finance needs estimated at over $2 trillion per year,[4] make it urgent to consider alternative mechanisms to expand the financing sources for sustainable development spending.

The international monetary system (IMS) further deepens these vulnerabilities through structural asymmetries. The pro-cyclical behaviour of capital flows toward EMDEs leads these countries to accumulate large foreign exchange reserves for precautionary purposes in case there is an abrupt interruption in international financing, tying up resources that could otherwise be used for productive investment and development. These dynamics not only constrain EMDEs' growth but also contribute to global instability and demand shortfalls.[5]

Special Drawing Rights (SDRs)[6] issuances present a concrete alternative to address these asymmetries and financing needs without deepening the debt

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[1] International Monetary Fund, "Debt Vulnerabilities and Financing Challenges in Emerging Markets and Developing Economies—An Overview of Key Data", *Policy Papers* 2025, 002 (2025).

[2] Particularly, net external debt transfers to low and middle income countries (excluding China) turned negative for the 2021-2023 period, which indicates that the amount that these countries paid in interest and principal during those years to service their external debt exceeded what they received in new disbursements. World Bank, "International Debt Report" (2024).

[3] Patricia Miranda, Veronica Serafini, Nathalie Beghin, et.al., "Special drawing rights (SDRs), a lifeline for the Global South and a boost to the global economy", T20 Policy Brief (2024).

[4] Climate Policy Initiative, "Global Landscape of Climate Finance 2024: Insights for COP29", (2024). Currently, commitments are embedded in the finance target of the New Collective Quantified Goal (NCQG), which was agreed last year at COP29 and seeks to scale up the climate financing to developing countries to at least USD 1.3 trillion per year by 2035, from a wide variety of sources including public and private, bilateral and multilateral, and alternative sources.

[5] International Monetary Fund, "Considerations on the Role of the SDRs", *Policy Paper* (2018); Bilge Erten and José Antonio Ocampo, "Building a stable and equitable global monetary system", DESA Working Paper, 118 (2012).

[6] Special Drawing Rights are interest-bearing international reserve assets created by the International Monetary Fund (IMF) in 1969 mainly to address global liquidity needs. SDR allocations provide IMF members with access on demand to *freely usable currencies* (i.e., members' currencies that are broadly used to pay for international transactions or widely traded in the principal exchange markets such as the US dollar, the euro, and Japanese yen) on an unconditional basis (no

crisis that many EMDEs are experiencing or negatively impacting their growth since SDRs uses are not subject to regressive conditionalities.[7] However, SDRs' design and allocation system pose significant limitations for their effective use, making SDRs one of the most underutilised instruments of international economic cooperation. This policy brief focuses on the specific challenge related to the SDRs allocation criterion.[8]

Challenges

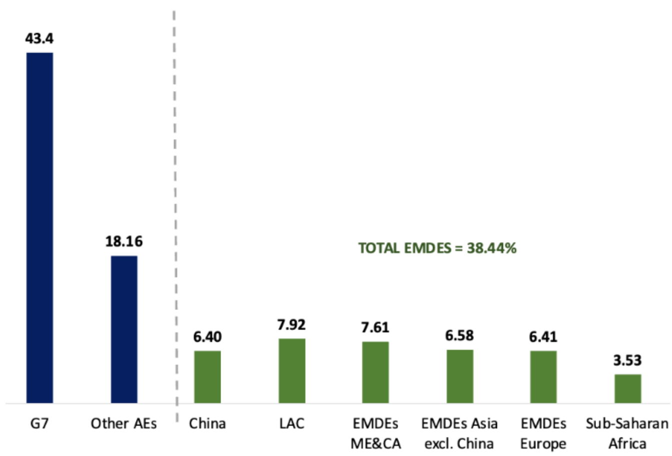
As per the SDR allocation procedure, countries receive a share of SDRs proportional to their actual quotas shares (AQS) in the International Monetary Fund (IMF). While this approach is consistent with the IMF's governance structure, it has important distributional consequences: advanced economies (AEs), which hold the largest quotas, receive the greatest share of any SDR allocation, regardless of their external financing needs. These countries are typically issuers of reserve currencies and do not face foreign exchange shortages, making them less likely to use their allocations.

condition is imposed on the economic policies of the country that uses its SDR allocation). Then, SDRs are not a currency but a claim. Exchanging SDRs for foreign currency entails paying an interest rate over the difference between SDRs' cumulative allocations and holdings.

[7] Cashman, Kevin, Andrés Arauz, and Lara Merling, "Special Drawing Rights: The Right Tool to Use to Respond to the Pandemic and Other Challenges", Center for Economic and Policy Research (2022).

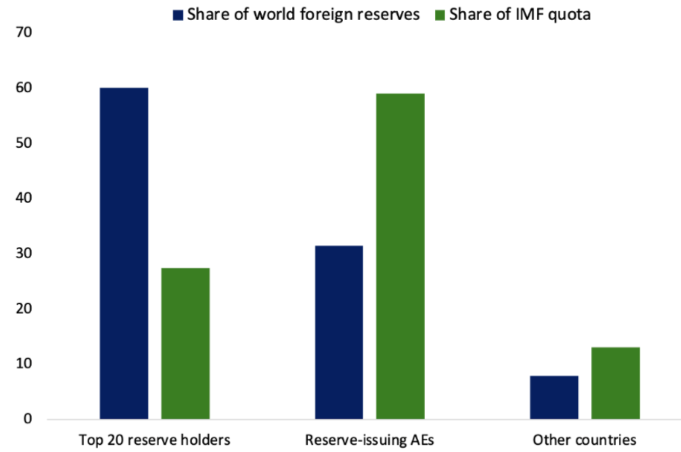
[8] There are several challenges related to the governance and use of SDRs. One of them is that SDR allocations have been infrequent and unpredictable, and have most recently been used only in response to global crises, such as the Global Financial Crisis and the COVID-19 pandemic. In this regard, there have been different proposals to address this issue, including establishing regular annual allocation (e.g., Truman, 2022). Others mention that there is an underutilization of SDRs, given not only to the allocation criteria but also to domestic regulations and to specific challenges related to rechanneling or donating SDRs (e.g., Paduano, 2024; Arauz and Vasic-Lalovic, 2024).
Edwin M. Truman, "The IMF should enhance the role of SDRs to strengthen the international monetary system", Peterson Institute for International Economics (2022); Stephen Paduano, "A State of Play on SDRs: What To Make of 2023, What to Watch in 2024", Finance for Development Lab (2024); Andrés Arauz and Ivana Vasic-Lalovic, "Three Years After SDRs Were Issued, Debt-Based SDR Rechanneling Has Failed", Center for Economic and Policy Research (2024).

Figure 1
Actual Quota Shares as percentage by regions



Note: Regions are categorized according to the 2024 WEO classification. AE: Advanced Economies, EMDE: Emerging Market and Developing Economies, LAC=:Latin America and the Caribbean, ME&CA: Middle East and Central Asia. Source: own elaboration based on 2024 IMF data.

Figure 2
Foreign exchange reserves and IMF Actual Quota Shares



Note: Share of world foreign exchange reserves only refers to 191 IMF member countries. Reserve-issuing AEs include Australia, Canada, Switzerland, Japan, the United Kingdom, European Union member countries, other AEs of the Euro Area, Japan and the US. The top 20 reserve holders exclude reserve-issuing AEs. Source: own elaboration based on 2024 and 2022 IMF data.

This has resulted in a striking mismatch between the distribution of SDRs and the countries most likely to use them. In the 2021 general allocation – totalling USD 650 billion – over 60% of SDRs were allocated to AEs, which already possess deep capital markets and substantial reserve buffers. In contrast, many low-income countries (LICs),[9] which faced acute fiscal and balance of payments (BoP) pressures during COVID-19, received only a small share (3.2%). EMDEs, particularly LICs, were the main users of SDRs. As of July 2023 – less than two years after the 2021 allocation – the ratio of cumulative SDR holdings (ie, the SDRs still held by a country) to cumulative allocations received from the IMF[10] stood at 88% for EMDEs excluding LICs and 54% for LICs. Moreover, a considerable number of EMDEs had

[9] In this policy brief, based on the IMF 2023 Assessment report, low-income countries are those eligible to use the Poverty Reduction and Growth Trust (PRGT).

[10] The cumulative allocation of SDRs refers to the total amount allocated by the IMF to a given country, while SDR holdings represent the amount of SDRs the country currently holds, which could be either lower or higher than the cumulative allocations received. Since countries can use SDRs in multiple ways — such as exchanging them for freely usable currencies, making payments to the IMF, or settling other international obligations —holdings may fall below the cumulative allocation, resulting in a holdings-to-allocations ratio below 1. Conversely, countries may also acquire additional SDRs by providing liquidity to other countries (freely usable currencies, e.g. US dollar, Japanese Yen, Euro) in exchange for SDRs, typically through the Voluntary Trading Arrangements (VTA) market. In such cases, holdings may exceed allocations, leading to a ratio above 1, mainly observed among AEs.

nearly depleted their holdings, with 33 countries recording ratios below 5%.[11] Meanwhile, for AEs the aggregate holdings-to-allocation ratio was 104% and most of them left their SDRs untouched, with only one (Greece) actively using them by the end of 2022.[12]

Recognising these disparities, the IMF and several member countries have pledged to reallocate unused SDRs from AEs to more vulnerable countries. In practice, however, reallocation has been limited[13] – constrained by political considerations and administrative and regulatory restrictions.

Moreover, there is an increasing misalignment between AQS and the ones resulting from the quota formula.[14] AQS are mainly determined by IMF governance and historical power relations and do not reflect members' relative sizes in the global economy.[15]

Therefore, this policy brief calls for a rethinking of SDR allocation criteria to harness the use of SDRs for crisis management and financing for development, considering a needs-based approach that relies on metrics of countries' financing needs and vulnerabilities.

[11] International Monetary Fund, "2021 Special Drawing Rights Allocation—Ex-Post Assessment Report", *Policy Papers*, 035 (2023).

[12] We exclude the use of SDRs for rechannelling purposes. IMF "2021 Special Drawing Rights Allocation—Ex-Post Assessment Report" (2023); Andrés Arauz and Francisco Amsler, "More SDRs for Latin America and the Caribbean: An Effective Tool in an Era of Multiple Crises", Center for Economic and Policy Research (2024).

[13] As of September 2024, only an estimated $6.5 billion out of the $ 100 billion pledged by G20 countries has been effectively rechanneled through the IMF's Resilience and Sustainable Trust (RST) and Poverty Reduction and Growth Trust (PRGT) facilities. Based on Ivana Vasic-Lalovic, "Three Years After SDR Were Issued, Debt-Based SDR Rechanneling Has Failed", Center for Economic and Policy Research (2024).

[14] International Monetary Fund, "Fifteenth General Review of Quotas—Quota Formula and Realigning Shares", Policy Paper, 007 (2021).

[15] Even a future realignment of quotas toward Calculated Quota Shares (the ones that result from applying the quota formula) would not necessarily prioritize countries with greater financing needs since 50% of the quota is determined by GDP.

Recommendations

When SDRs were created (1969), their original mandate was to support the Bretton Woods monetary system as a supplementary reserve asset. As stated in the IMF's Articles of Agreement (AoA), their objective was "to meet long-term global needs, *as and when it arises, to supplement existing reserves assets*".[16] This goal was unmet as the Bretton Woods system shortly after collapsed and SDRs played a minor role. Then, there was a renewed interest in SDRs given the absence of a gold standard and concerns over USD exchange rate volatility,[17] leading to an amendment of the AoA stating SDRs as the principal reserve asset of the IMS.[18] Yet, after the second SDR allocation (1971-1981), there was a lack of consensus over the role of SDRs and their use largely stalled. It was only in 2009, during the global financial crisis, and in 2021, in response to the COVID-19 pandemic, that SDRs reemerged as a key crisis-response tool. In particular, the 2021 allocation broadened SDRs' role,[19] as the IMF[20] considered other SDR uses beyond holding them as reserve buffers in response to BOP fragilities, including using SDRs to respond to the COVID-19 pandemic and its consequences[21] and to support a resilient, inclusive, and sustainable recovery.[22]

Considering SDRs' current and potential roles, we propose rethinking the allocation criteria of future issuances. The goal is to enhance SDRs' role in crisis

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[16] According to IMF AoA (Article XVIII, Section 1), "In all its decisions with respect to the allocation and cancellation of special drawing rights the Fund shall seek to meet the long-term global need, as and when it arises, to supplement existing reserve assets in such manner as will promote the attainment of its purposes and will avoid economic stagnation and deflation as well as excess demand and inflation in the world".

[17] IMF, "Considerations on the Role of the SDR" (2018).
[18] IMF AoA, Article XXII.
[19] Lazard, "Rechannelling SDRs in a Responsible and Efficient Way", Policy Brief (2022).
[20] The Executive Directors asked the IMF staff to prepare a Note to guide the treatment and use of the general allocation of SDRs. International Monetary Fund, "Proposal for a General Allocation of Special Drawing Rights", *Policy Papers*, 049 (2021).
[21] For instance, by using SDRs to finance additional spending in healthcare.
[22] The IMF 2021 Note mentioned in particular the use of SDRs to address the pre-pandemic trends of low productivity growth and rising inequality.

management and to harness their potential for financing sustainable development.

Building on past reform proposals, we suggest the following guiding principles for future SDR allocations:

i) SDRs should be allocated disproportionately, relative to AQS, to countries with the greatest financial needs and economic vulnerabilities.
ii) The allocation criteria should incorporate measures of financial need, economic vulnerability, and liquidity constraints rather than relying solely on AQS.
iii) The criteria should be transparent, simple and easy to implement. Following the IMF quota formula guiding principles,[23] it should be feasible to implement and based on timely, high-quality and widely available data.
iv) Proposals must consider their institutional and political feasibility. Reforming SDR allocation criteria entails amending the AoA, which requires 85% of the voting power for approval.[24] The likelihood of adoption is determined by major IMF shareholders, particularly the US and Europe, which hold de facto veto power.[25]

When considering the role of SDRs in crisis management, SDR allocations should consider BoP's current and potential needs. There is a precedent:[26] the IMF's quota formula includes a variable called "Variability",[27] which was introduced as

[23] International Monetary Fund, "Fifteenth General Review of Quotas—Quota Formula and Realigning Shares", Policy Papers, 007 (2021).
[24] According to the AoA (Article XXVIII), 85% of the voting power of the Board of Governors and 75% of members' countries is required for the approval of an amendment to the AoA.
[25] While they do not possess a formal veto, they effectively exercise one given the size of their quota shares, as each holds over 15% of the IMF's total voting power.
[26] One major challenge in agreeing on a metric or set of metrics for allocating SDRs is the need for a criterion that can gain the support of key stakeholders, such as the United States and the European Union. Even if newly proposed metrics may offer a better fit for the reform's objectives, a more politically feasible option might be to use metrics that are already under consideration (or being used) by the IMF.
[27] Variability refers to the variability of current receipts and net capital flows measured as the standard deviation from a centered three-year trend over 13 years of the sum of *current receipts* and *net capital flows or minus the financial account balance*. Net capital flows relate to cross-border transactions of the financial account in all external financial assets and

a proxy for countries' vulnerability to BoP shocks and potential demand for funds.[28] This implies that variability should aim to favour EMDEs, particularly LICs that are more vulnerable to BoP shocks and are more in need of IMF resources.[29] However, empirical studies[30] found no evidence linking variability to such demand or vulnerabilities. Furthermore, when assessed in relation to GDP, this metric tends to favour small economies, which include not only LICs but also high-income economies like Iceland, Luxembourg, and Singapore.

Ocampo[31] proposed tying SDR allocation to countries' demand for international reserves, for example, by adjusting AQS of middle and low-income countries by a factor reflecting their reserve needs (in terms of GDP) relative to high-income countries and compensating LICs for strictly redistributive purposes. However, this approach will not necessarily guarantee an SDR allocation based on financial needs since, for instance, Switzerland (reserves-to-GDP ratio equal to 89.8%), Singapore (68.7%) and Japan (29.5%) would receive disproportionate allocations under this criterion despite limited financial needs.[32] The approach could be improved by considering reserve adequacy metrics since they measure a country's potential foreign exchange liquidity needs, particularly in adverse circumstances, by considering a country's reserve position relative to particular risk factors.[33] Traditional metrics include reserves to import, broad money or short-term debt.[34]

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liabilities (i.e., the financial account balance based on the "analytic presentation" of the balance of payments). This concept excludes reserve assets, credit and loans from the Fund, and exceptional financing.

[28] International Monetary Fund, "Fifteenth General Review of Quotas" (2021).

[29] Trevor Lwere, Rob Floyd, and Hannah Ryder, "Reimagining the IMF's Quota System and Representation in Africa's Interest", T20 Policy Brief (2024).

[30] International Monetary Fund, "Quota Formula - Data Update and Further Consideration", Policy Paper (2013); International Monetary Fund, "Quota Formula - Data Update and Further Considerations", Policy Paper (2014).

[31] José Antonio Ocampo, "Financing for Development: The Global Agenda", Columbia University (2025); Erten and Ocampo, *"Building a Stable and Equitable Global Monetary System" (2012)*.

[32] The ratio uses data for the year 2023 and was computed as total reserves minus gold over GDP (at market exchange rates, current USD) based on World Bank Data.

[33] International Monetary Fund, "Guidance Note on the Assessment of Reserve Adequacy and Related Considerations", Policy Paper (2016).

[34] A more comprehensive measure that could be explored is the IMF's Assessing Reserve Adequacy (ARA) metric, which accounts for a broader set of risks[34] and is tailored to different types of EMDEs. According to the IMF "Guidance Note of

Beyond crisis response, SDRs also hold potential as a tool for development finance. In this role, structural vulnerabilities should be considered aiming to mitigate the medium- and long-term impact of potential future shocks.[35] Cornier and Wagner propose as a measurement the structural universal vulnerability index (SUVI) of the Commonwealth Secretariat[36] that captures a country's vulnerability to external economic and natural shocks, climate change and socio-political conflicts, as well as its structural resilience[37] to respond to these shocks. The authors demonstrate that incorporating SUVI[38] into allocation criteria could redirect SDRs toward the world's poorest and most vulnerable nations. Other authors also supported the idea of including countries' vulnerabilities to climate shocks[39] and considering countries' per capita income into allocation frameworks.[40]

Conclusion

There is an opportunity to revamp the role and use of SDRs by reforming the allocation criteria of future issuances considering a transparent and data-driven

Reserve Adequacy" (2016), this indicator is intended to cover four sources of risks: i) the potential loss of export income (due to a drop in external demand or terms of trade shock), ii) the risk of resident outflows (measured through broad money), iv) rollover risks (measured through short-term debt), and iv) the risk of non-resident equity and MLT debt outflows (other liabilities). The weights given to each component are based on the 10th percentile of observed outflows from emerging markets during exchange market pressure episodes. In addition, the measure is adjusted if the country is dollarized, has capital controls in place, or is a commodity exporter/importer. According to this metric and IMF's International Financial Statistics (for the year 2023), countries with reserves below adequate, relate to low coverage of imports (on average, 4 months), however, this was not the case for the coverage of short-term debt and broad money. Hence, an approach could be explored combining traditional measures of reserve adequacy with the reserve-to-ARA metric ratio.

[35] Alban Cornier and Laurent Wagner, "Using a Vulnerability Index to Simulate a Reallocation of SDRs?", Fondation pour les études et recherches sur le développement international (FERDI) Policy Brief, B229 (2022); Patrick Guillaumont, Sylviane Guillaumont Jeanneney, and Laurent Wagner, "How to Allocate New External Financing to African Countries? The Vulnerability Challenge. A Briefing in Response to the Paris Summit on Financing African Economies", FERDI Policy Brief, B217 (2021).

[36] Ruth Kattumuri and Travis Mitchell, "The Commonwealth Universal Vulnerability Index: For a Global Consensus on the Definition and Measurement of Vulnerability", Commonwealth Secretariat (2021).

[37] The structural resilience index takes into account measurements of human and physical capital, per capita income, infrastructure and demographic factors, among others.

[38] The authors also include other variables in their proposals such as population, GNI per capita, and balance of payment current account credit per capita.

[39] Brahima S. Coulibaly and Eswar Prasad, "A Reform Proposal for a Fit-For-Purpose International Monetary Fund", T20 Policy Brief (2023).

[40] Ocampo, "Financing for Development: The Global Agenda" (2025).

framework based on countries' financing needs and structural vulnerabilities. This would ensure that SDRs are deployed where they can have the greatest macroeconomic and developmental impact. It would also complement ongoing initiatives to rechannel SDRs.

Given that the G20 concentrates over 60% of the IMF's voting power, their engagement is critical for initiating changes to SDR allocation criteria (as was the case in past SDR allocations). Furthermore, it is a space where the main agreements related to the guiding principles of the reform could be made. Particularly, the International Financial Architecture working group of the G20 Finance Track is uniquely placed to initiate discussions on SDRs' challenges and explore potential solutions.

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