

IMF gives developing countries a substantial boost amid delta variant crises

By: Emerging Markets Team | August 25, 2021

Boston - The International Monetary Fund (IMF) made the largest allocation of Special Drawing Rights (SDRs) in its history —\$650 billion — at the start of this week. According to the IMF, the allocation, which is an interest-bearing international reserve asset that can be exchanged for dollars or other major currencies with Central Banks, is a significant shot in the arm in the ongoing fight to recover from the COVID-19 pandemic.

The SDR allocation will provide additional liquidity to the global economy by supplementing countries' foreign exchange reserves and reducing their reliance on the capital markets. Emerging markets countries, in particular, will benefit from the additional liquidity. While investor appetite for emerging markets debt remains robust year-to-date with \$50.2 billion in inflows as of August 20, 2021, the SDR allocation from the IMF will be an important additional funding source.

Developing nations are the top beneficiaries

SDR Allocations are based on countries' quotas with the IMF, which are based predominantly on GDP. The IMF estimates that \$275 billion will be allocated to emerging and developing countries. Of that, low-income countries will receive about US\$21 billion, which is equivalent to as much as 6 percent of their GDP in some cases.

Emerging markets countries are positioned to greatly benefit from this allocation because of the percentage increase in liquidity relative to their existing reserves. Among the countries that would benefit the most are Zimbabwe, Sudan, Zambia, Suriname, Ethiopia, Sri Lanka and Ecuador. The inflow of funds should more than double some of these countries' international reserves.

For example, Ethiopia and Zambia will see some of the largest percentage increases in reserves resulting from the SDR allocation. In Argentina, the government has already stated its intent to use the resources from the SDR allocation to repay principal and interest payments due to the IMF for its current loan program later on this year.

IMF moves forward despite mounting controversy

Ethiopia, one of the biggest beneficiaries on a percentage basis, receives funding despite having been sanctioned by the US government for engaging in war and genocide. Belarus received its allocations despite the country's ongoing efforts to suppress democracy. U.S. Treasury Secretary Janet Yellen had called on the IMF to exclude Belarus from funding. However, as members of the IMF, the IMF asserts that these countries have a right to these allocations.

The IMF did block Afghanistan from this week's allocation following pressure from the Biden Administration, however, following the collapse of the government and the takeover by the Taliban. Member countries and the international community help guide the Fund. The lack of clarity in the international community regarding the recognition of the government creates uncertainty.

There was some discussion around the possibility of pre-conditions attached to the allocation of SDRs. Although there are no official pre-conditions attached to disbursement, it should be noted that some countries do face certain directives from the IMF on use of funds. For example, in Uganda, the new allocation has been written into higher international reserve targets under the country's IMF program, accompanied by a warning that a decision to monetize the SDRs for budget financing would need to be discussed by both parties first.

Other criticism of the SDR allocations include that most of the money will go to developed countries because the allocation is based on countries' quotas at the IMF, which are based in part on GDP. Talks are in place to develop a system through which wealthy nations can channel their SDRs to poorer and vulnerable countries. This redistribution could provide additional much needed financial support to developing nations and the IMF notes that additional SDRs could be used to fight climate related challenges. The spring 2021 IMF meeting revealed that the IMF has expanded their agenda and social concerns, such as climate change, are a top priority for the Fund.

Bottom line: This record allocation by the IMF should help build confidence and foster resilience and stability in the global economy at a time when the delta variant threatens the world's recovery. How the IMF monitors how recipients use these allocations will continue to be an ongoing discussion.



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