How Effective Was Assistance to the Vulnerable Countries During the Pandemic? Comparing the Debt Service Suspension Initiative and Special Drawing Rights

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Abstract

This paper compares the actual and potential resources derived from the G20's Debt Service Suspension Initiative and the actual and potential resources from International Monetary Fund's 2021 allocation of Special Drawing Rights. These programs were two main sources of support for 73 vulnerable countries during height of the COVID-19 pandemic. For these countries, Special Drawing Rights provided much greater potential support when compared to the Debt Service Suspension Initiative. Special Drawing Rights deployed more actual resources as well. When these programs are evaluated from the perspective of the countries receiving assistance, Special Drawing Rights are found to have several characteristics that are more desirable. As such, as a tool, Special Drawing Rights have several advantages that should be taken into account during discussions about policy responses to global challenges in the future.

Key words: International Monetary Fund, SDR, Special Drawing Rights, DSSI, Debt Service Suspension Initiative
J.E.L. classification: E02, E60, F33, F53

1. Introduction

The COVID-19 virus, which spread rapidly in early 2020, killed nearly 7 million people to date, according to the World Health Organization (WHO, 2023). Apart from this devastating human toll, the pandemic also threw vulnerable countries into even more precarious economic situations, starving governments of revenue as spending for vaccines, personal protective equipment, and social programs became necessary. Growth projections plunged, leading the International Monetary Fund (IMF) to call the downturn the worst since the Great Depression (Gopinath, 2020). Health, education, and living standards, as measured by the Human Development Index, fell for the first time since 1990 (UNDP, 2022).

Vulnerable countries experienced various shocks due to the pandemic. For example, many countries dependent on tourism, an important source of hard currency, saw that industry shut down overnight, while countries with large export markets experienced demand, supply chain, and production issues. Generally, as money moved out of vulnerable countries, they faced either challenges with maintaining reserves and/or keeping their local currencies stable. These problems can compound rapidly, leading to difficulties servicing debt, exchange rate pressures that made imports expensive, and/or a hollowing out of the state's capacity to spend (Cashman et al., 2022). The world needed new tools to provide resources and liquidity to struggling countries that also did not add to their debt loads.

Facing these issues, the Group of 20 launched the Debt Service Suspension Initiative, or DSSI (G20 Information Centre, 2020). The poorest countries, according to the United Nations' definition or those eligible for International Development Assistance, that also have debt outstanding to the World Bank or IMF, were eligible for the DSSI. This amounted to 73 countries in total. From May 2020 to December 2021, the G20 says the DSSI suspended $12.9 billion in official debt payments to 48 countries (World Bank, 2022).

The IMF’s Board of Directors also initiated a program to assist countries facing challenges from the pandemic. In August 2021, the IMF allocated $650 billion worth of Special Drawing Rights, or SDRs, to all of its members. A unique tool, SDRs are reserve assets that can be exchanged into hard currency (usually the United States dollar) if a country has a need to do so. The IMF would then find another member country that would agree to accept SDRs in exchange for hard currency. SDRs are not loans but carry a non-compounding interest rate that has a 0.05 percent floor and is 3.9 percent currently (IMF, 2023a). $209 billion was deployed to low- and middle-income countries in 2021, and these resources were used extensively in 2021 and 2022.

Apart from using them as reserves on a balance sheet (which requires no action), 104 vulnerable countries used SDRs, either by exchanging them for hard currency, using them to service IMF debt, or for fiscal purposes. For example, 69 countries used SDRs for fiscal purposes amounting to $80.4 billion (Arauz and Cashman, 2022). These uses are not necessarily additive, however, due to different accounting methods.

This paper will compare these two programs based on their potential impact, assessment of the actual impacts, and the characteristics of each program, as well as provide background on how SDRs work. This information will be of use to policymakers and governments in evaluating potential responses to future crises.

2. Theoretical background

In 1969, the IMF created SDRs — a reserve asset — as a supplement to the reserves of its member countries. As a reserve asset, SDRs do not represent debt or loans, but function as a unit of account at the IMF level. IMF member countries, and some other entities such as development banks, have accounts at the IMF denominated in SDRs. The IMF creates a market for buying and selling SDRs among holders by asking well-resourced countries to commit to accepting SDRs in exchange for hard currency, or currencies that have value globally.

Right now, the value of the SDR is determined by a basket of five currencies, but the United States dollar holds the most significance (IMF, 2023b). When countries exchange SDRs for hard currency or pay the IMF itself, their SDR holdings fall below its allocation, or the total amount of SDRs they been given over time. These countries must pay an interest rate on the difference between their holdings and their total allocation. This interest paid is given to countries that have a surplus of SDRs, or more holdings than their respective allocations. The interest rate is determined regularly but varies from a floor of 0.05 percent. It is just under 4 percent today (IMF, 2023a). The interest rate, even at nearly 4 percent, is desirable because it is lower than the market rate many countries would pay and because the interest accrued is non-compounding.

In total, there have been four allocations of SDRs during the program’s existence (IMF, 2023c). Before the pandemic, the last time an allocation occurred was in 2009, when $250 billion in SDRs aimed to provide liquidity globally during the Great Recession.

The process for allocating SDRs is administratively a quick one — once political will exists among its membership. This decision must include key members such as the United States, which has the power to stop an allocation of SDRs on its own. US law also limits SDR allocation to under just over $650 billion, unless the allocation is approved by US Congress (Cashman et al., 2022). One of the main impediments to the allocation in 2021 was that the United States’ initially opposed a new allocation.

3. Research methodology

Potential DSSI use was extrapolated from the calculations provided by the World Bank (World Bank, 2022). Actual DSSI use was also found via the World Bank at the conclusion of the DSSI program, yet this did not include breakdowns by country for the 48 countries that participated in the program or indicate whether this figure include the sole private creditor that participated.

Potential SDR use (from the 2021 allocation) was found in Cashman et al. (2022); actual SDR use was taken at the one-year mark by Arauz and Cashman (2022), published in August 2022.

The 68 DSSI-eligible countries with available data in the World Bank's International Debt Statistics database (World Bank, 2023) comprised the sample by which aggregates and country-by-country data was compiled. This assumes that the 68-country sample includes all 48 participants in the DSSI program.

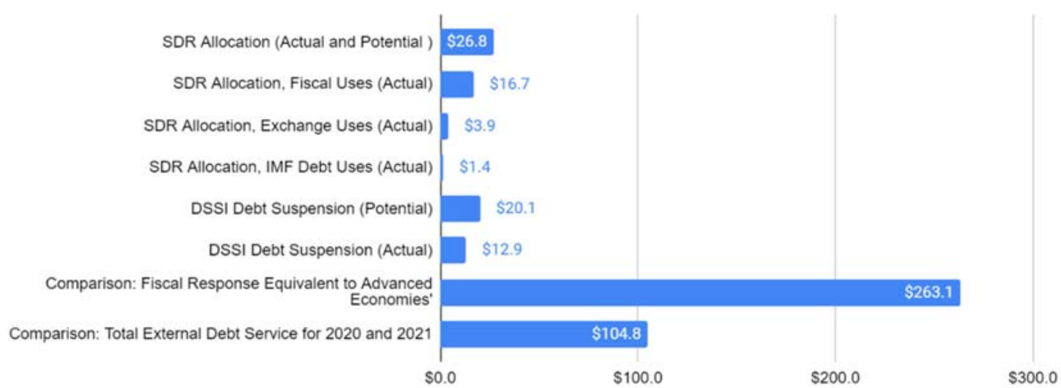
For comparison purposes, total external debt service was also found in the International Debt Statistics database. Data aggregating the fiscal responses to the pandemic by advanced economies was also collected for comparison purposes from the IMF's fiscal response database (IMF, 2021). This data was then adjusted so it was in proportion to the aggregate size of the economies in the sample of 68 countries.

4. Findings

For the sample of 68 countries with data available both for DSSI and SDRs, Figure no. 1 compares the aggregate actual and potential use for each program. SDRs allocated to this group of countries amounted to $26.8 billion at the time of allocation. This is both an actual and potential figure since SDRs were automatically added to member countries' accounts at the IMF in August 2021, at the time of the new allocation. Thus, as reserve assets, this is a use, although no action was taken by these countries at that point. Research by Arauz and Cashman, shows that this sample of countries used SDRs in the amount of $16.7 billion for fiscal uses, $3.9 billion for exchange uses (acquiring hard currency), and $1.4 billion for IMF debt relief (Arauz and Cashman, 2022).

The SDR allocation was significantly greater than the potential DSSI debt suspension, which was $20.1 billion. The actual estimates suspension of debt via DSSI from the G20 was only $12.9 billion, also significantly less than the overall SDR allocation and the fiscal uses of SDRs by these countries. The $12.9 billion figure may even be an overstatement. The World Bank states only $8.9 billion of official debt suspended under DSSI (World Bank, 2022b).

Figure no. 1. Aggregate Amount of Potential and Actual Use of DSSI and SDRs for 68 DSSI-Eligible Countries, in Billions USD



Sources: Authors' calculations based on (Arauz and Cashman, 2022)

Both programs are inadequate, however, when considering the amount of resources advanced economies created by themselves to respond to the pandemic. Although the countries in this sample do not have the fiscal space to create resources like advanced economies, if they did, they would have created $263.1 billion for fiscal use to respond to the pandemic, when scaled for the aggregate size of their respective economies. Likewise, although DSSI and SDRs were tools deployed to temper the effects of the pandemic, the most optimistic reading of their actual impact is dwarfed by the total external debt service for 2020 and 2021 for the countries in this sample, which comes to a whopping $104.8 billion.

Table no. 1 shows the data from Figure no. 1 broken down by country. Although aggregate actual use of DSSI is available, it is not available by country. Of the 68 countries, 60 of them used SDRs in some way other than simply having the allocation on their books. This drops to 53 when excluding 15 countries with marginal (under $5 million) SDR use.

Table no. 1. Amount of Potential and Actual Use of SDRs and Potential Use of DSSI for 68 DSSI-Eligible Countries, in Millions USD

Country	SDR Allocation (Actual, Potential Use)	SDR Fiscal Uses (Actual)	SDR Exchange Uses (Actual)	SDR IMF Debt Uses (Actual)	DSSI Debt Suspension (Potential)
Afghanistan	$442	$0	$0	$6	$73
Angola	$1,010	$497	$0	$83	$2,900
Bangladesh	$1,456	$0	$0	$183	$615
Benin	$169	$166	$0	$4	$33
Bhutan	$28	$0	$0	$15	$144
Burkina Faso	$164	$162	$0	$0	$33
Burundi	$210	$0	$80	$0	$8
Cabo Verde	$32	$32	$32	$0	$34
Cambodia	$239	$0	$0	$0	$378
Cameroon	$377	$213	$213	$1	$672
Central African Republic	$152	$140	$140	$4	$14
Chad	$191	$184	$184	$7	$102
Comoros	$24	$24	$24	$0	$5
Congo, Dem. Rep.	$1,455	$503	$503	$0	$276
Congo, Rep.	$221	$278	$278	$0	$333
Côte d'Ivoire	$888	$873	$0	$186	$150
Djibouti	$43	$0	$43	$1	$142
Dominica	$16	$0	$0	$2	$8
Ethiopia	$410	$404	$404	$5	$685
Fiji	$134	$0	$0	$0	$30
Gambia, The	$85	$20	$0	$2	$13
Ghana	$1,007	$330	$0	$123	$355
Grenada	$22	$0	$0	$3	$11
Guinea	$292	$150	$284	$5	$104
Guinea-Bissau	$39	$38	$0	$2	$7
Guyana	$248	$243	$243	$0	$28
Haiti	$224	$110	$110	$6	$128
Honduras	$341	$336	$336	$4	$53
Kenya	$741	$728	$0	$99	$1,190
Kosovo	$113	$111	$0	$1	$8
Kyrgyz Republic	$242	$0	$0	$13	$118
Lao PDR	$144	$0	$70	$0	$619
Lesotho	$95	$0	$0	$5	$14
Liberia	$353	$347	$0	$10	$5
Madagascar	$334	$334	$0	$9	$19
Malawi	$189	$189	$181	$5	$37

Maldives	$29	$29	$28	$0	$229
Mali	$255	$255	$0	$10	$102
Mauritania	$176	$176	$166	$9	$218
Moldova	$235	$221	$221	$14	$63
Mongolia	$99	$0	$0	$6	$134
Mozambique	$310	$305	$0	$0	$565
Myanmar	$705	$0	$0	$5	$794
Nepal	$214	$211	$0	$0	$51
Nicaragua	$355	$0	$0	$0	$43
Niger	$180	$177	$0	$11	$55
Nigeria	$3,351	$3,294	$0	$38	$325
Pakistan	$2,772	$2,725	$0	$433	$5,404
Papua New Guinea	$359	$353	$0	$0	$73
Rwanda	$219	$215	$0	$22	$27
Samoa	$22	$0	$0	$2	$18
São Tomé and Principe	$20	$20	$20	$1	$6
Senegal	$442	$434	$0	$4	$339
Sierra Leone	$283	$56	$0	$14	$17
Solomon Islands	$28	$0	$0	$0	$2
Somalia	$223	$84	$84	$0	$39
St. Lucia	$29	$0	$0	$0	$7
St. Vincent and the Grenadines	$16	$0	$0	$1	$6
Tajikistan	$238	$0	$0	$2	$104
Tanzania	$543	$0	$0	$0	$463
Timor-Leste	$35	$0	$0	$0	$0
Togo	$200	$197	$0	$0	$49
Tonga	$19	$0	$0	$0	$14
Uganda	$493	$242	$0	$0	$231
Uzbekistan	$752	$0	$0	$1	$526
Vanuatu	$32	$0	$0	$2	$13
Yemen, Rep.	$665	$0	$0	$9	$281
Zambia	$1,335	$1,313	$281	$0	$529

Sources: Authors' calculations based on (Arauz and Cashman, 2022)

5. Conclusions

These programs illustrate two different approaches to tackling the twin health and economic crises posed by the pandemic. DSSI provided official debt suspension to countries that applied, while ensuring that the net present value of the loans stayed constant despite the suspension. Clearly, the program was attractive to a set of countries that were eligible for it since 48 of 73 countries received debt suspension via the program. Although DSSI was supposed to serve as a model for private creditors, which represent around half of external debt globally and 25 percent of debt for this sample, only one private creditor voluntarily participated (World Bank, 2022).

In contrast, the 2021 SDR allocation provided reserve assets to all IMF member countries, regardless of their need for the resources. While this may seem counterintuitive as richer countries also receive resources, these resources are not useful to countries in stronger economic positions. Thus, SDRs automatically provide resources to the countries that need it, within the structure of the IMF system, where countries are treated more like peers rather than debtors.

(While there are democratic deficits within the IMF system, it is inherently more democratic than the G20.)

Table no. 2 compares various relevant characteristics of both programs.

Table no. 2. Select Characteristics of SDR and DSSI Systems

Characteristics	**SDR**	**DSSI**
Eligibility	All 190 IMF members	73 eligible countries
Uptake	Of 68 in sample, 60 countries	48 countries
Conditionality	No, apart from showing need via a self-assessment	Yes, various conditions, e.g. commitment to take on no new debt
Use	Countries may use SDRs in a variety of ways that extend the resources above the allocated value. They may exchange them for any of the currencies in the SDR basket, in any amount (provided a counterparty is available); they may use them to pay the IMF directly; and as property of governments (except when otherwise indicated by local laws), they may use them in fiscal accounts without exchanging them.	Temporary debt suspension only, a debt standstill
Focus	In 2021, providing countries with liquidity via a flexible tool to address macroeconomic problems and specific problems related the COVID-19 pandemic; this could be extended for various other global challenges	Suspension of official debt only, which is a fraction of total debt and did not include private creditors formally
Cost	SDR allocations are cost-free, and if they are exchanged, they benefit both parties as the purchaser of SDRs receives the interest paid by the seller. Users pay an interest rate that is non-compounding and is usually below market rate. Even with extensive interest rate increases globally in 2022 and 2023, the rate sits below 4 percent. Further research could explore the risk of excessively tight interest rate policy on the SDR interest rate.	Designed to be net present value neutral to creditors, payments deferred under new terms
Duration	Although users pay a non-compounding interest rate if they hold fewer SDRs than the amount allocated to them, this can continue indefinitely	DSSI, which started in May 2020, wound down in December 2021
Institutional Framework	IMF's system of governance, which includes all members but gives disproportionate influence to advanced economies, especially the United States (via the US Treasury or the US Congress)	G20, excluding target countries
Mobilization	Can be quickly mobilized and deposited in IMF accounts	Can be mobilized quickly via G20, but countries must meet conditions and go through an application process
Effectiveness	SDRs are distributed to all member countries but cannot be wasted because countries that do not need them do not find their use attractive	Excludes vulnerable countries that do not meet specific criteria or countries that do not wish to apply for whatever reason
Sanctions-compliant	Yes, the IMF follows its member countries' guidance on recognition, or suspension of recognition, of governments of member countries. Additionally, member countries need not transact with specific countries.	Yes, creditor governments do not need to suspend the debt of a particular debtor government if they were ever in this unlikely situation

Source: Authors' analysis based on (Cashman et al., 2022)

This discussion does not intend to imply that programs like the DSSI are not valuable. Indeed, vulnerable countries clearly benefited from both programs. Intervention to aid vulnerable countries was also necessary at many different levels due to the inability of the private sector to respond to global challenges. But DSSI only created temporary fiscal space via a debt standstill for a small portion of vulnerable countries' debt service; they must continue payments on the rest.

With an eye to the future, SDRs seem to be more advantageous. SDR allocations have many benefits that may be applicable to old challenges, like the potential global debt crisis on the horizon, and new challenges, like the ones posed by climate change, that do not neatly fit into a debt framework. SDRs also allow for liquidity to be increased over the long term, not just for a temporary period.

Indeed, the 2021 SDR allocation has kickstarted a discussion within civil society about new allocations of SDRs: over 150 organizations have signed onto support another allocation of SDRs (CEPR, 2022). There is interest in rechanneling SDRs allocated to richer countries to poorer countries, while preserving the unique aspects of the tool (Arauz, 2022). In addition, the United Nations has proposed the IMF "[automate] SDR issuance in a countercyclical manner or in response to shocks, with allocations based on need."

The SDR system has proven its usefulness to its users, vulnerable countries. Time will tell if there is political will to firmly integrate this unique tool into the global financial architecture.

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