SDR Allocations in the Middle East: Helpful, but No Silver Bullet

by Jonah Shrock (/experts/jonah-shrock)

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Brief Analysis

Various governments have made good use of last year's unprecedented IMF allocation, but the Ukraine war, ongoing debt issues, and other economic problems are a reminder that the region cannot sidestep deeper reforms indefinitely.

Last year, the International Monetary Fund dispersed the largest allocation of Special Drawing Rights (SDRs) in its history, more than twice the amount granted in the previous five decades combined. About 7% of the August 2021 allocation went to the Middle East, providing significant relief to countries whose foreign reserves had been strained by the COVID-19 pandemic. In the year since then, governments in the region have exchanged their SDRs for around $910 million worth of IMF debt relief and $6.3 billion worth of foreign currency.

What Are SDRs?

SDRs can be thought of as a currency created by the IMF, with a value that the institution determines in relation to a weighted basket of the U.S. dollar, euro, yuan, yen, and British pound sterling. Unlike normal currencies, however, SDRs cannot be held by private individuals. Rather, they act as a stable asset in a country's international reserves and can also be held by the IMF and a select few "prescribed holders"—mainly multinational development institutions such as the Arab Monetary Fund. For comparison, SDRs make up 2% of global reserves while the U.S. dollar makes up 57%.

Distributing the Major 2021 Allocation

Since 1969, the IMF has conducted four general SDR allocations and one special allocation, each time dispersing amounts in proportion to countries' respective ranks in the IMF quota system. The August 23, 2021, allocation was by far the largest ever—in all, roughly SDR 660 billion has been allocated in the program's history, but 456 billion of this total (equivalent to $650 billion) was allocated last August alone. At the time, officials described the unprecedented move as a response to urgent financing needs in the wake of the pandemic.

Approximately $400 billion worth of last year’s allocation went to wealthy countries, while $230 billion went to middle-income countries and $20 billion went to low-income countries. The G7 and G20 pledged to channel $100 billion worth of their SDRs through two IMF funds designed to help low-income countries and address structural challenges (e.g., climate change). So far, however, none of the promised rechanneling has occurred.

The Middle East portion of the 2021 allocation was equivalent to around $47 billion. Although the amounts distributed to needy countries such as Lebanon ($865 million) were dwarfed by what wealthy countries such as the United States received ($35 billion), the allocation still provided the region with significant liquidity at a difficult time.

How Have Middle Eastern Countries Used Their SDRs?

Since the allotment, various security and economic challenges have further disrupted the balance of payments for countries in the region. As mentioned above, the large allocation was originally spurred by the global need for liquidity amid the pandemic, but food and fuel prices have skyrocketed since then amid rising U.S. interest rates, a strengthened U.S. dollar, and the tanking of Middle Eastern currencies such as the Turkish lira and Egyptian pound. The situation has drained foreign exchange reserves in the affected countries as the cost of imports has increased. Globally, 60% of low-income countries are debt distressed or at high risk of falling into that category. This in turn has affected how governments use their SDR allocations, including in the Middle East.
Thus far, seven countries in the region have tapped into their 2021 SDRs, with five of them using nearly all of their allocation. Egypt has used the most, in part to pay down its status as the largest IMF debtor in the world apart from Argentina, with $17.7 billion outstanding (https://www.imf.org/external/nr/tad/bal/mr02.aspx?type=TOTAL) and $2.6 billion worth of SDRs in service relief for 25 eligible low-income countries (https://www.imf.org/external/np/fin/tad/taddr2.aspx?datekey=2004-01-12&reportdate=2004-01-12). Meanwhile, Iraq has used SDRs to help pay off its IMF debt entirely—it had an estimated $604 million (https://www.imf.org/external/np/fin/tad/exporta.aspx?memberkey1=%202046&datekey1=2021-07-31&dateyear=2021&category=EXC) in outstanding debt to the organization in July 2021, but it has since brought that figure down to zero for the first time since 2004 (https://www.imf.org/external/np/fin/tad/extend2.aspx?datekey1=2004-01-12&reportdate=2004-01-12), in part by tapping $184 million worth of SDR debt relief. Most other Middle Eastern countries have likewise used the allocation to lower their IMF debt.

One exception is Jordan, whose debt to the institution has actually grown by over $300 million since 2021. This partly reflects the kingdom’s decision to use just 5% of its allocation on debt relief compared to 94% exchanged for currency. Overall, Middle Eastern countries currently hold around SDR 8.0 billion ($10.4 billion) less than what they have been allocated over the years—a debt that will cost the region about SDR 131 million ($169 million) per year in interest. Yet these amounts are relatively small compared to government budgets. For example, Iraq’s 2021 budget called for $89 billion in spending, which dwarfs its SDR interest bill of SDR 43 million ($56 million).

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Conclusion

For most Middle Eastern countries, the plus-size 2021 SDR allocation served as a nice bonus rather than a lifesaver. In Saudi Arabia, for example, the government was not in desperate need of liquidity, but the extra assets helped it make large deposits in the central banks of Egypt (https://www.arabnews.com/node/1958636/business-economy) and Pakistan (https://www.ft.com/content/77e7f0ce-9ddd-ta0c-4c5f-8e2764480f2), expanding the kingdom’s economic influence in both countries. In other cases, governments used the allocation to supplement their existing plans for paying down debt to the IMF.

In contrast, Lebanon and Egypt were so desperate for liquidity that they quickly used up their entire allocations. Of course, both countries are facing much more fundamental problems than a mere short-term need for liquidity. Lebanon is experiencing one of the worst economic crises (https://www.worldbank.org/en/news/press-release/2021/05/01/lebanon-sinking-into-one-of-the-most-severe-global-crises-in-history), while Goldman Sachs recently estimated (https://www.bloomberg.com/news/articles/2022-08-01/goldman-a-15-billion-view-of-egypt-imf-needs-too-high-for-2021) that Egypt may need to secure a $15 billion package from the IMF even after using $2.6 billion worth of SDRs in the past year. Solving these problems will require fundamental economic reforms.

Moreover, when the IMF made the allocation in 2021, it could not have foreseen the Russian invasion of Ukraine or the global debt crisis that ensued. The latter challenge will require major debt restructuring and cooperation from China, the world’s largest creditor. And while SDRs will likely be part of this solution, they are not a silver bullet.

Jonah Shrock is a former research assistant with The Washington Institute’s Koret Project on Arab-Israel Relations.
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