



A Synthetic Currency Can Help the Real Economy

John Williamson argues that major, regular issues of special drawing rights (SDRs), created to satisfy part of the growing need for international liquidity, could help reconcile payments objectives.

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Steve Weisman: This is Steve Weisman at the Peterson Institute for International Economics. John Williamson, senior fellow at the Institute, is here to discuss a subject that he has written a couple of papers on and studied a long time, but is not one of the more well-understood subjects in international finance and currency—special drawing rights, or SDRs. John, thanks for taking the time to talk to us about this subject today.

John Williamson: It's a pleasure.

Steve Weisman: What are special drawing rights and why are they important as the globe struggles to climb out of a worldwide recession?

John Williamson: SDRs are a synthetic unit that was created by the International Monetary Fund (IMF). There was debate when they were first created in the late 1960s about whether they should be called a new form of international money or whether they were simply credit. And to avoid answering this question, they were given this hideous name of "special drawing rights," which implied that one didn't need to answer the question because it wasn't specific either way on that issue.

There were then a couple of allocations in the early days, and then the SDR more or less hibernated and everyone, including even me, forgot about it for about 30 years. Then thinking about the London summit last April and what could be done, the idea came up of a major allocation of SDRs as a way of helping especially the smaller countries to be able to afford expansionary policies and to overcome the recession.

Steve Weisman: There are roughly how many SDRs in existence?

John Williamson: I think it's just over 20 billion at the present stage.

Steve Weisman: SDRs are a synthetic currency but based on a relationship with real currencies or a basket of currencies?

John Williamson: Yes, indeed. This was actually one of the changes that I helped make in the early 1970s when I was in the IMF and the world had moved to virtual exchange rates. And it really didn't make any sense to have the SDR just tied to the dollar when all the other currencies were floating in terms of the dollar.

Steve Weisman: Which currencies are they linked to?

John Williamson: Nowadays, it's an average of the US dollar, the euro, the pound sterling, and the Japanese yen, and with relative modest weights for the last two. But all the same, they are sufficiently important in world trade that it still felt desirable to retain them in the basket.

Steve Weisman: As you pointed out just now, in London, an expansion of these SDRs was authorized. What happened after London? Have countries availed themselves of these SDRs in their recovery efforts?

John Williamson: The SDRs were duly allocated and made available to countries, I think, at the very end of August. And it's now part of history that countries have received these additional SDRs and whether some of them have adopted more expansionary policies than they otherwise would have done as a consequence, no one is in a position to say.

Steve Weisman: Why can't we say?

John Williamson: Because of background noise, which goes on all the time. There's no controlled experiment. Some countries didn't receive SDRs, and other countries were denied them. And the countries that didn't receive them were North Korea and Cuba, I think, and maybe Taiwan, I guess. They're non-members of the IMF. And those aren't sufficient to make a controlled experiment to see how much additional expansion was created by the receipt of these extra SDRs.

Steve Weisman: But they were a piece of the solution, it appears, to the global recovery. And the global recovery does seem to be occurring. One doesn't follow the other without proof, but can we surmise that they may have contributed to the progress that we're seeing?

John Williamson: They may have. But as I say, one really has no proof. Presumably, some of the efforts clearly were influential. I mean, one can see that countries like China recovered very rapidly, and on the basis of their expansionary package, taken already last November. And then other countries like the United States had expansionary fiscal packages, much larger than the SDR on occasion.

And there's no question that some of these fiscal packages were relevant and also the fact that inventories were run down very much in relation to sales, that was certainly a contributory factor. So there were a number of factors, and I don't doubt that the SDR, on occasion, was one of them. But if some skeptic comes along and says you have no proof of that, well, they're right. I mean, I don't have proof of it.

Steve Weisman: What is the G-20 looking at right now in terms of its future policy on the SDRs—not just the G-20, but the IMF and other international institutions? And in that context, you've written in your papers that the SDRs may become an element and possibly even a basis for some kind of new international monetary system. How far along might we be on such a path?

John Williamson: I think that it's very important that the international system decides that this is not just a once-off occurrence—this SDR occasion—that is going to be forgotten about

in the future. But instead, it's going to be regarded as a regular part of the very large increases in demand of dollar reserves that had been manifested in the recent years. And so, I would like to see SDR allocations, at least as large as that of this year, being repeated in future years as a regular part of creating additional liquidity and thereby reducing the necessity for the United States to incur balance-of-payments deficits to expand liquidity.

Steve Weisman: In other words, this would diminish the desire of exporting countries to build up the big dollar reserves that some feel contributed to this—what I guess Bernanke and others call global savings glut. Do you share that view?

John Williamson: I certainly share the view that if one supplies reserves in this form, that reduces the need to build up reserves in other forms. Now, it's possible that some of the countries are more motivated by the desire to expand trade and exports than they are to actually accumulate reserves. And one can't exclude that possibility. I don't think that it's going to apply through a majority of countries, and I don't think that even the countries to which it may have applied in the past, like China, are going to continue with that path. I think they realize now the problems that come through being a major dollar creditor.

Steve Weisman: What can we expect at the next round of meetings at Pittsburgh? Or would you expect decisions to be made later this year or next year at other forums?

John Williamson: I'm afraid that I've not read anything that leads me to believe that this is going to be on the agenda for Pittsburgh. And as I say, I think there's a strong case for it, but I don't think that the case is being argued at the moment. And in the absence of somebody willing to take the lead in arguing it, it will go by default.

Steve Weisman: What is the Obama administration's position on this?

John Williamson: The Obama administration is very willing to adopt the suggestion [of] a large SDR allocation, interpreted as a once-off thing, as a way of helping the world get out of recession. But whether they are also convinced about the case for regular SDR allocations, we don't yet know.

I think it's inherent in the logic of their position, because they certainly have been arguing very strongly that the United States is no longer to act as consumer of last resort. And if there's a continuing demand to build up reserves and this US determination not to continue running such expansionary policies, the two can only be reconciled by something like an SDR on occasion.

Steve Weisman: Finally, John, explain to me something that you and Fred Bergsten, the director of the Institute, have studied and written about, which is the possibility of something called the Substitution Account that would facilitate this move toward the SDRs playing a more dominant role in the international currency regime.

John Williamson: The Substitution Account essentially is a way of allowing countries to achieve their reserve increases in the form of SDRs, but ex post rather than ex ante, instead of having a new injection of international liquidity to which countries have to react

by changing their policies. One says, okay, given the policies that happened in the past, some countries have accumulated a lot of dollars and they're going to be able to exchange those dollars for SDRs in the Substitution Account, which would then come to hold claims on the United States. And instead of all the member countries of the Fund, it would be holding just claims on the United States, but the liability side of its balance sheet would be the same. Namely, it would be issuing SDRs for other countries to hold.

Steve Weisman: Do you think this is in the offing?

John Williamson: I have not seen any suggestion that the larger countries are particularly interested in this solution. I think China might be interested, and maybe in the future [they] are going to push it. But I haven't seen evidence that they're pushing it so far.

Steve Weisman: John, thank you for joining us and explaining something that may only materialize in the future, but at least we need to understand it now. Thanks a lot.

John Williamson: Well, it's a pleasure. Thank you.

