A Modest Proposal for the G20

A group of international scholars and policy-makers met in Beijing on 18th of March 2011, to discuss reforms in the international monetary system. There is a general consensus that there is a need for fundamental reforms in that system, which, even if it has not caused recent imbalances and instability in the global economy, has certainly proved ineffective in addressing them. While such reforms will require extensive discussion and deliberation, the consensus of the Beijing Group was that there was a modest proposal which could be adopted this year by the G20: a limited expansion of the current SDR system. This modest proposal, while limited in scope, could be play an important role in initiating discussions of deeper reforms and which would, at the same time, make a modest contribution to restoring the world's fragile economy to health, helping to achieve the aim expressed in the G20 Pittsburgh declaration for a "*strong, sustainable and balanced growth*".

We suggest that the role of Special Drawing Rights (SDRs) be increased, both by new SDR issues and by increasing the role of the SDR in IMF lending. This measure would build on the enlightened suggestion made at a previous G20 meeting in April 2009 in London to issue SDRs equivalent to 250 billion dollars, which was then quickly implemented. The G20 could suggest that the International Monetary Fund issues a significant amount of SDRs during the next three years. We would suggest, for example, an issue of 150 billion to 250 billion SDRs annually.

Such a measure would have a number of positive effects. Firstly, it would reduce the recessionary bias in the world economy, especially during – and in the aftermath of – crises. Many countries continue to accumulate high levels of reserves for precautionary motives, especially to avoid future crises associated to reversals on their capital and trade accounts. The crisis has taught countries that those with large reserves are in a better position to weather the vicissitudes of the international financial markets. While such reserve accumulations help protect countries, at the same time, in certain periods they reduce global aggregate demand. Given its relatively small scale, the issue of SDRs would make up only partially for these deficiencies in global aggregate demand, but even these limited amounts would help sustain and accelerate recovery of the world economy without leading to inflationary pressures. It is also now widely recognized that the build up of reserves contributes to global imbalances, and by reducing the need for countries to set aside funds for reserves, it would also facilitate some reduction of global imbalances.

This additional issuance of reserves could ideally be accompanied by further measures to increase the effectiveness of SDRs. One such measure would be to treat the unused SDRs that countries hold as "deposits" in the IMF, which the Fund could then use to finance its lending programmes. This should be understood as the first step to integrate the "general resources" and the "SDR" accounts into a single IMF account, and to increase the role of the SDR in IMF transactions so it eventually becomes the main – or even only – mechanism for IMF financing. During a declared crisis, IMF lending should be totally financed by new SDR issues in unlimited amounts.

A working group could be established to study other reforms that would enhance further global financial stability and address other global economic and financial objectives. For instance, alternative systems of SDR allocation, with a greater proportion of SDRs issued given to the countries actually demanding the reserves, mainly the developing countries, might contribute to global growth and stability. An advantage of this modest proposal is that it would not prejudice the outcomes of the working group. The issuance of additional SDRs while making a contribution to enhancing global stability today would not alter in any fundamental way existing monetary arrangements.

We suggest that this proposal be a subject of discussion at the meeting in Nanjing.

The G20 showed its effectiveness in responding to the crisis in 2008 and 2009. The question today is whether, with the passing of the moment of crisis, with the emergence of large divergences in both perspectives and circumstances, the G20 can demonstrate the leadership the world needs in addressing its ongoing critical problems. There is a serious risk of disillusionment if there is a failure to take concrete action. This model proposal would prove the continued role of G20 leadership to ensure greater stability and more sustained growth in the world economy.

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